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AUDIT MANUAL RELEASE 3.0

DECEMBER 1993

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Department of Energy

Memorandum

DATE: December 20, 1993

REPLY TO:
ATTN OF: IG-30

SUBJECT: Release 3.0 of the Audit Manual

TO: All OA Staff

Attached is release 3.0 of the Audit Manual. You will note many changes and some reorganization of material in this release. Most of the changes are indicated by a vertical line in the right margin.

Release 3.0 is effective immediately. Comments or suggestions for future enhancements to the Audit Manual are welcome and should be directed to the members of the Committee on Audit Standards, Policies and Procedures.

In addition, we are providing the Handbook for Auditors-In-Charge: Leadership for Audit Excellence on the accompanying computer disk.

Gordon W. Harvey
Assistant Inspector General
for Audits

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITS

AUDIT MANUAL

Release 3.0

OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITS
AUDIT MANUAL

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Change Control Sheet

ABBREVIATIONS/ACRONYMS USED IN THIS MANUAL

ACAP	Audit Career Advisory Panel
ACP	Audit Control Point
ADP	Automated Data Processing
AIC	Auditor-In-Charge
AICPA	American Institute of Certified Public Accountants
AIGA	Assistant Inspector General for Audits
AIGI	Assistant Inspector General for Investigations
AIG/IA	Assistant Inspector General for Inspections and Analysis
AIGP	Assistant Inspector General for Policy, Planning and Management
AO	Office of Audit Operations (formerly AMD)
AP ³	Office of Audit Policy, Plans and Programs (formerly PDTSD)
ARM	Assistant Regional Manager
CAS	Cost Accounting Standards
CASB	Cost Accounting Standards Board
COR	Contracting Officer's Representative (formerly COTR)
CPA	Certified Public Accountant
CPE	Continuing Professional Education
CRO	Capital Regional Audit Office
DAIG	Deputy Assistant Inspector General
DAIG/AO	Deputy Assistant Inspector General for Audit Operations
DAIG/AP ³	Deputy Assistant Inspector General for Audit Policy, Plans and Programs
DARTS	Departmental Audit Reports Tracking System
DCAA	Defense Contract Audit Agency
DEAR	Department of Energy Acquisition Regulations
DOE	Department of Energy
E-Mail	Electronic Mail
ERO	Eastern Regional Audit Office
FAR	Federal Acquisition Regulations
FMFIA	Federal Managers' Financial Integrity Act
GAGAS	Generally Accepted Government Auditing Standards
GAO	U.S. General Accounting Office
IG	Inspector General

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IGDBMS	IG Database Management System
IPA	Independent Public Accountant
M&O	Management and Operating (contractor)
MRL	Management Representation Letter
PC	Personal Computer
OA	Office of Audits
OJT	On-the-Job Training
OMB	Office of Management and Budget
OIG	Office of Inspector General
PCIE	President's Council for Integrity and Efficiency
QCR	Quality Control Review
SAAIG	Special Assistant to the Associate Inspector General
SAS	Statement on Auditing Standards
TF&R	Tentative Findings & Recommendations
TIMS	Training Information Management System
VANEA	Voucher Accounting for Net Expenditures Accrued
WRO	Western Regional Audit Office

CHAPTER 1INTRODUCTION TO THE AUDIT MANUALA. PURPOSE OF THE MANUAL

This Manual consolidates into one document the policies, procedures, standards, technical guidance and other techniques to be followed by the Assistant Inspector General for Audits (AIGA) and staff in planning and conducting audit work within the Department of Energy (DOE) and in preparing related reports on behalf of the Office of Inspector General (OIG).

B. APPLICABILITY

All auditors in the Office of Audits (OA) and auditors under contract to the AIGA are required to follow the policies and procedures contained in this Manual for all audit work.

C. RELATIONSHIP OF MANUAL TO EXTERNAL STANDARDS

The audit standards, policies, and procedures to be followed in executing OA's mission were compiled from a variety of sources. This Manual is intended to be consistent with external standards and to ensure that financial and performance audits conducted by or on behalf of the OA are fair, professional, objective and reliable.

1. Government Auditing Standards. The "Government Auditing Standards," 1988 Revision, issued by the Comptroller General of the United States, contains standards for audits of government organizations, programs, activities, and functions, and of government funds received by contractors, nonprofit organizations, and other nongovernmental organizations, and shall apply to all AIGA audit work. These standards are referred to as "Generally Accepted Government Auditing Standards" (GAGAS) or, more informally, the U.S. General Accounting Office (GAO) "Yellow Book."

2. American Institute of Certified Public Accountants. The American Institute of Certified Public Accountants (AICPA) has issued various "Statements on Auditing Standards" (SAS) that have been incorporated by reference in the GAO Yellow Book for financial and financial related audits.

3. President's Council on Integrity and Efficiency. The President's Council on Integrity and Efficiency (PCIE) has promulgated standards--i.e., "Quality Standards for Federal Offices of Inspector General," issued January 1986--that apply to governmental audit activities and are consistent with the standards issued by the Comptroller General. The PCIE has also developed standards and detailed guidance for conducting external quality control reviews of OIG audit operations.

4. Office of Management and Budget Circulars. The Office of Management and Budget (OMB) has issued various circulars that require audits to be con-

ducted in accordance with GAGAS, or that otherwise affect how audits of DOE operations and activities are to be conducted. These circulars include:

- o OMB Circular A-73, (Revised) "Audit of Federal Operations and Programs," issued August 1, 1983.
- o OMB Circular A-102, (Revised) "Grants and Cooperative Agreements with State and Local Governments," issued March 3, 1988.
- o OMB Circular A-110, "Grants and Agreements With Institutions of Higher Education, Hospitals, and Other Nonprofit Organizations," issued July 30, 1976.
- o OMB Circular A-123, (Revised) "Internal Control Systems," issued August 4, 1986.
- o OMB Circular A-128, "Audits of State and Local Governments," issued April 12, 1985.
- o OMB Circular A-133, "Audits of Institutions of Higher Education and Other Nonprofit Organizations," effective March 16, 1990. Circular A-133 supersedes Attachment F, subparagraph 2h, of Circular A-110.

5. The Inspector General Act of 1978. The Inspector General Act of 1978 (IG Act), as amended, requires that audit work conducted by the federal inspectors general, as well as audit work conducted by nonfederal auditors on their behalf, comply with the GAO Yellow Book standards.

D. STRUCTURE OF MANUAL

This Manual is divided into seven major sections, as follows:

1. Part I -- General. Part I of the Manual includes chapters on auditing in DOE and general audit policies.
2. Part II -- Fieldwork. Part II of the Manual includes chapters on fieldwork policies, planning, conducting the audit, workpaper support, and advanced audit techniques.
3. Part III -- Reporting. Part III of the Manual includes chapters on reporting policies and standards, report organization, report staffing and distribution, quality control procedures, and audit resolution and follow-up.
4. Part IV -- Contract Audits. Part IV of the Manual includes chapters on policies and procedures for contract auditing.
5. Part V -- Federally Assisted Programs. Part V of the Manual discusses policies and procedures for audits of Federally Assisted Programs.
6. Part VI -- Integrated Contractor Audits. Part VI of the Manual includes chapters on policies and procedures for auditing all aspects of integrated contractor operations.

7. Part VII -- Administrative. Part VII of the Manual includes chapters on general policies and procedures for office administration, personnel management, professional development, and travel.

E. UPDATES TO THE MANUAL

This Manual is intended to be a basic reference document for all OA guidance and instructions. To ensure that it is most useful as a basic reference document, it should be kept current and as relevant to the way audits are actually done as possible. The primary mechanism to accomplish this will be a standing "Committee on Audit Standards, Policies and Procedures."

1. Committee on Audit Standards, Policies and Procedures. A standing Committee on Audit Standards, Policies and Procedures will be responsible for reviewing suggested revisions to the Manual and for preparing updates for AIGA review and approval.

a. Suggestions - Suggestions for revisions to the Manual are welcomed and should be brought to the attention of the Deputy Assistant Inspector General for Audit Policy, Plans and Programs (DAIG/AP³) or to members of the Committee on Audit Standards, Policies and Procedures.

b. Membership - Each Deputy Assistant Inspector General (DAIG) and Regional Manager will designate one person to serve on the Committee. If a member is not available for a particular meeting, a DAIG or Regional Manager can designate an alternate to serve on the Committee.

c. Responsibilities - The Committee will meet as often as necessary to review suggested revisions to the Manual and to prepare updates for AIGA review and approval. The Committee does not have to convene at one location if it can carry out its responsibilities through other means, such as using conference calls, electronic mail, facsimile machines, or other means to conduct its review in a timely and efficient manner. The DAIG/AP³ will oversee Committee activities and coordinate AIGA review and approval of revisions to the Manual proposed by the Committee.

2. Other Changes. Occasionally, changes to the Manual may be required within extremely short time frames. These types of changes should be infrequent and made only for matters of such significance or urgency that they cannot wait until the next meeting of the Committee on Audit Standards, Policies and Procedures. In such cases, the proposed change should be submitted to the DAIG/AP³ with a cover memorandum attached stating why the originator believes the change should be released immediately. Final approval for immediate release will be sought from the AIGA.

3. Distribution Procedures. Each auditor will be provided with one printed copy of the Manual and one electronic copy (on 3.5 inch diskette). The diskette contains the entire Manual, including exhibits. These printed and electronic copies will be updated in accordance with the following procedures.

a. DAIG/AP³ Issues Changes - The DAIG/AP³ is responsible for

issuing changes and updates to the Manual that have been approved by the AIGA. Revisions to the Manual will be issued with serially numbered and dated transmittals that identify the changes.

b. Changes Issued to All Offices - All changes and updates to the Manual will be issued through Regional Managers, Assistant Regional Managers (ARMs), and Audit Directors. Audit Directors are responsible for ensuring that an office copy of the Manual (including diskette) is kept up to date.

c. Major vs. Minor Revisions - When major revisions are made to the Manual, each auditor will be provided with both the printed changes and a new diskette. For minor revisions--i.e., a few pages or less, each auditor will be provided only the printed changes. However, electronic changes will be distributed to each Audit Director who will be responsible for ensuring that a master diskette is available to all auditors for duplication.

d. Immediate Changes - If the need for an immediate change to the manual has been approved by the AIGA, the change will be sent via file transfer to all audit offices. Audit Directors will be responsible for assuring that hard copies of the change are distributed immediately to all staff for inclusion in the Manual.

(1) Confirmation. Confirmation of distribution will be required from Audit Directors back to AP³ within 3 working days of the date of the file transfer.

(2) Incorporation. The change will be formally incorporated into the next distributed release of the Manual.

e. Change Control Sheet - Auditors are responsible for keeping their printed and electronic copies current. The Change Control Sheet in the back of the Manual should be used by each holder to ensure that changes to the Manual are recorded and to help identify any missing changes.

f. Mailing List - AP³ maintains a mailing list that contains all OA employees, contractor employees, certain DOE officials, management and operating (M&O) contractor internal audit staffs, and others who need or have requested copies of the Manual. Anyone on the list will automatically receive updates to the Manual. Others wishing to be added to the mailing list should contact AP³ at the following address:

U.S. Department of Energy
Office of Inspector General
Office of Audit Policy, Plans
and Programs (IG-32)
1000 Independence Avenue, SW
Washington, DC 20585

Attn: Audit Manual

CHAPTER 2AUDITING IN THE DEPARTMENT OF ENERGYA. SCOPE OF CHAPTER

This chapter provides information on the organization and structure of the Department, the OIG, the AIGA, and related background information useful for understanding auditing in DOE.

B. DEPARTMENTAL OVERVIEW

DOE conducts activities in a wide variety of scientific, technical, revenue generating, and financial support areas. Following is an overview of the wide range of activities supported by DOE subdivided into areas that best describe the nature of the effort:

- o *Research and Development* includes scientific and technical activities being performed in a number of areas, including energy, basic science research, and atomic energy defense;
- o *Defense Production and Support* is concerned with the production of weapons and special nuclear materials;
- o *Waste, Remedial Activities, and Oversight* combines civilian and defense activities responsible for the processing, transportation, and ultimate disposition of radioactive and hazardous waste, for environment, health and safety oversight, and for environmental remedial action. However, this category does not include those ongoing environmental and safety activities which are directly funded within specific program areas such as nuclear energy, energy research, and defense;
- o *Business Enterprises* combines activities of the Department that generate revenues and store or market energy products, and are managed like a business;
- o *Grants and Other Energy Functions* groups non-research conservation grant programs and such activities as energy information and regulation; and
- o *Departmental Management* includes the various overhead activities of the headquarters and field organizations.

As of 1993, about 161,000 personnel worked at DOE facilities throughout the country employed either directly or indirectly by the DOE. Approximately 141,000 of the employees work for the contractors that operate the Department's laboratories and industrial facilities. The remaining 20,000 employees are Federal workers who, among other things, provide administrative services and programmatic direction and oversight of the work done for the DOE by its operating contractors. See exhibit A (not on disk) for a DOE organizational chart, exhibit B (not on disk) for a chart of DOE field relationships, and exhibit C (not on disk) for a map of DOE field facilities and operations.

DOE's fiscal year 1993 budget request was \$19.4 billion, including \$7.5 billion for defense, \$5.3 billion for environment, \$3.2 billion for energy supplies, \$3.0 billion for research, and \$0.4 billion for management and other activities. The auditable dollars, however, are far greater than the \$19.4 billion annual budget. Total auditable dollars, at about \$36 billion, also include revenues, carryover funds, and other dollars not included in the budgeted amounts.

C. AUTHORITY AND RESPONSIBILITIES

The Inspector General (IG) is generally responsible for all financial and performance auditing within DOE. This responsibility, however, does not supplant the authority of Departmental officials to make programmatic reviews of individual programs and enforce regulatory functions. Specific authority and responsibilities are discussed below.

1. Statutory Authority. The DOE Organization Act, Public Law 95-91, as amended (42 U.S. Code 7138) established an OIG in DOE. Public Law 100-504 transferred the authority of the DOE OIG to the IG Act, as amended (Title 5, U.S. Code, App. 3).

a. Appointment of Assistant Inspector General for Audits - The IG Act states that each IG shall, in accordance with applicable laws and regulations governing the civil service, appoint an AIGA who shall have the responsibility for supervising the performance of auditing activities relating to programs and operations of the establishment.

b. Preparation of Semiannual Reports - The IG Act also requires each IG to prepare semiannual reports summarizing the activities of the Office during the immediate preceding six-month periods ending March 31 and September 30. Such reports include

- o a description of significant problems, abuses, and deficiencies relating to the administration of programs and operations of such establishment disclosed by such activities during the reporting period;
- o a description of the recommendations for corrective action made by the Office during the reporting period with respect to the significant problems, abuses, or deficiencies identified;
- o an identification of each significant recommendation described in previous semiannual reports on which corrective action has been completed;
- o a summary of matters referred to prosecuting authorities and the prosecutions and convictions which have resulted; and
- o a summary of each report made to the head of the establishment;

c. Distribution of Semiannual Reports - In accordance with the IG Act, the IG's semiannual reports are to be furnished to the Secretary of Energy and transmitted by him to the appropriate committees or subcommittees

of the Congress within 30 days after receipt of the report. The IG is also required to report immediately to the Secretary when he/she becomes aware of particularly serious or flagrant problems, abuses, or deficiencies relating to the administration of programs and operations of the Department.

2. Nonstatutory Responsibilities. In addition to the statutory reporting responsibilities summarized above, the IG has additional nonstatutory reporting responsibilities.

a. PCIE Requirements - The PCIE was established by Executive Order 12301, dated March 26, 1981, to provide leadership for Governmentwide activities to reduce waste, fraud, or abuse and to improve the economy and efficiency in Federal programs and operations. Its membership consists of the statutory IGs and representatives of other selected agencies. The PCIE requires the IG to

- o report on specific reviews of DOE programs and operations that may be of interest to the PCIE, and
- o participate in and report on general Government-wide reviews where DOE is one of the sample agencies.

b. Cognizant Federal Audit Agency - The IG is responsible for reports on audits of a particular contractor or grantee where DOE has been designated as the cognizant audit agency for a (1) contractor by virtue of predominance of work, or (2) a grantee under the provisions of OMB Circulars A-102, A-110, A-128, and A-133.

c. Requests from Other IGs - From time to time, requests for audit assistance are received from the IGs of other departments and agencies. These requests impose additional nonstatutory reporting responsibilities.

D. OIG ORGANIZATION AND RESOURCES

The IG is the principal advisor to the Secretary concerning the promotion of economy and efficiency in the administration of, and the prevention and detection of fraud, abuse, and irregularities in, programs and operations of the Department, including the Federal Energy Regulatory Commission.

1. Departmental Relationships. The OIG supervises, coordinates, provides policy direction for, and conducts audit, investigative, and inspection activities relating to the promotion of economy and efficiency in the administration of, and the prevention and/or detection of fraud or abuse in, programs and operations of the Department. The IG reports to the Secretary of Energy and the Deputy Secretary of Energy. In addition, the IG is required to submit reports concerning fraud, abuses, other serious problems and deficiencies to the Congress via the Secretary on a semiannual basis. The placement of the OIG within the Department is depicted in exhibit exhibit A (not on disk), DOE Organization Chart.

2. Organizational Structure and Functions. The OIG consists of four major elements: (1) the Office of the Assistant Inspector General for Audits (otherwise known as the Office of Audits (OA)), (2) the Office of the Assistant Inspector General for Investigations (AIGI), (3) the Office of the As-

sistant Inspector General for Inspections and Analysis (AIG/IA), and (4) the Office of the Assistant Inspector General for Policy, Planning and Management (AIGP). The OIG's major functions include the following.

- o Supervises, coordinates and provides policy direction for audit, investigative, and inspection activities related to the promotion of efficiency and economy in the administration of, and the prevention or detection of fraud or abuse in, programs and operations of the Department and its contractors.
- o Recommends policies for and conducts, supervises, and/or coordinates other activities carried out or financed by the Department for the purpose of promoting economy and efficiency in the administration of and preventing and detecting fraud and abuse in, the programs and operations of the Department.
- o Recommends policies for, and conducts, supervises, or coordinates relationships between the Department and other Federal agencies, State and local government agencies, and other nongovernmental entities with respect to (1) all matters relating to the promotion of economy and efficiency in the administration of, or the prevention and detection of fraud or abuse in, programs and operations administered or financed by the Department, and (2) the identification and prosecution of participants in such fraud or abuse.
- o Recommends action to correct problems, abuses, and deficiencies noted in the course of audits, inspections, and investigations.
- o Monitors and reports on the progress of implementing actions to correct problems, abuses, and deficiencies.
- o Keeps the Secretary and the Congress fully and currently informed concerning fraud and serious abuses, problems, and deficiencies relating to the administration of the Department, its programs, and operations.

E. OFFICE OF AUDITS STRUCTURE AND RESOURCES

This Office provides policy direction and supervises, conducts and/or coordinates all internal and contracted audit activities for all Departmental programs and operations, including those conducted under contracts and grants as well as those performed by Departmental employees. This Office is mandated by statute. The OA consists of two Headquarters elements and three Regional audit offices, as depicted in the following chart:

1/ Includes the ADP and Technical Support Division

2/ Federal Energy Regulatory Commission

The types of audits performed by OA, and the organization and function of each of its major offices--i.e., the two Headquarters elements and the three regional offices--are discussed below.

1. Types of Audits. In general, the audits performed by or at the direction of OA can be classified as financial and performance audits. Financial audits include financial statement and financial related audits of DOE's contractors and grantees. Performance audits include economy and efficiency and program audits.

a. Financial Statement - During this type of audit, the auditor determines (1) whether the financial statements of an audited entity present fairly the financial position, results of operations, and cash flows or changes in financial position in accordance with generally accepted accounting principles, and (2) whether the entity has complied with laws and regulations that may have a material effect upon the financial statement.

b. Financial Related - Financial related audits include determining (1) whether financial reports and related items, such as elements, accounts, or funds are fairly presented, (2) whether financial information is

presented in accordance with established or stated criteria, and (3) whether the entity has adhered to specific financial compliance requirements. Financial related audits include audits of contracts, grants, financial systems (e.g., payroll systems), computer-based systems, financial information (e.g., statement of cash receipts), and fraud or other illegal acts which could affect an entity's financial position. Audits of internal control systems and structure over accounting, financial reporting, and transaction processing would also be considered financial related.

c. Economy and Efficiency - Determines (1) whether the entity is acquiring, protecting, and using its resources (such as personnel, property, space) economically and efficiently; (2) the causes of inefficiencies or uneconomical practices; and (3) whether the entity has complied with laws and regulations concerning matters of economy and efficiency.

d. Program Audits - Includes determining (1) the extent to which the desired results or benefits established by the legislature or other authorizing body are being achieved; (2) the effectiveness of organizations, programs activities, or functions, and (3) whether the entity has complied with laws and regulations applicable to the program.

2. Office of Audit Policy, Plans and Programs. The Office of Audit Policy, Plans and Programs (AP³) provides the AIGA with the resources and specialized knowledge and experience to comply, in part, with the mandates of the IG Act to supervise, coordinate, and provide policy and direction for auditing of the programs and operations of the Department. This office is OA's single focal point for audit policy guidance, and for audit planning, budget support and preparation. This office also provides program development analytical services and automatic data processing (ADP) technical support to all OA organizational elements. The DAIG/AP³ reports to the AIGA.

a. General Policy Group - AP³'s general policy group is unstructured, with senior level personnel supervising junior level personnel on a project team basis. Its major functions are as follows:

- o Advises the AIGA on audit policies and procedures. Prepares and publishes policy memoranda and operating handbooks for all OA elements. Develops AIGA positions on regulations, rulings and other audit issues.
- o Develops and updates audit guidelines, procedures and strategies. Provides executive direction to workload planning and scheduling systems.
- o Provides program guidance in terms of audit targets and priorities for use by OA field entities in preparing their annual work plans and audit schedules.
- o Develops OA training policy and coordinates career development plans and OA training programs.
- o Coordinates OA efforts within DOE and maintains liaison with external audit agencies.

- o Evaluates activities of all OA audit operating elements against plans and assures that professional standards are maintained in all audit activities.
- o Reviews Departmental Policy decisions, Comptroller General decisions and regulations of the Department of Treasury, OMB, General Services Administration and other Federal agencies for applicability to OA audit policies and procedures.
- o Prepares Requests for Proposals (RFPs) for audit support services and coordinates with Office of Procurement through contract issuance.
- o Interfaces with OA field elements on Management Information Systems audit requirements and problems.
- o Prepares budget data to support budget requests for OA. As part of this function, develops and maintains a model for estimating audit resource needs.

b. ADP and Technical Support Division - Within AP³, the ADP and Technical Support Division has the following major functions.

- o Proposes, directs, and performs audits of information technology-based programs, activities, and operations, including audits of sensitive application systems and/or sensitive computer operations, throughout the Department.
- o Ensures implementation of audit standards, procedures, and guidelines consistent with the standards established by the Comptroller General of the United States for all auditing activities performed within the ADP and Technical Support Division.
- o Provides technical advice and assistance to auditors in the course of their reviews in (1) extracting or analyzing data from Departmental or contractor computer systems and/or (2) dealing with complex issues that involve information technology.
- o Devises and directs the use of innovative computer-assisted audit techniques.

3. Office of Audit Operations. The Office of Audit Operations (AO) provides the AIGA with the resources and specialized knowledge and experience to comply, in part, with the mandates of the IG Act to supervise, coordinate and provide policy direction for auditing of the programs and operations of the Department, including the operations of contractors and grantees. AO is responsible for providing oversight of financial (financial statement and financial related) and performance (economy and efficiency and program) audits. It represents the AIGA in dealings with officials who are responsible for DOE programs, coordinates activities between the three regional offices, and coordinates IG audit activities with the PCIE and other audit organizations. AO provides guidance for, coordinates, evaluates, and ensures progress of audits conducted by all OA organizational elements and cognizant contractor performed audit projects nationwide.

The Deputy Assistant Inspector General for Audit Operations (DAIG/AO) reports to the AIGA. AO functions are augmented by two Directors who generally specialize in the areas of financial audits and performance audits.

a. Financial Audits - The Director for Financial Audits provides the DAIG/AO with the means for planning, developing, and coordinating financial and financial related audits of the major functional areas of the Department that involve accounting and budgetary systems, and representing the DAIG/AO in dealing with officials who are responsible for managing these activities. Specific functions are to:

- o Provide guidance to the DAIG/AO on the development of DOE accounting systems that meet standards established by the Comptroller General of the United States;
- o Review designated DOE financial statements in accordance with applicable generally accepted government auditing standards and report results to appropriate levels;
- o Develop overall plans for and coordinate the performance of multi-location reviews of financial management operations throughout the Department and its contractors and grantees;
- o Provide assistance to AP3 in the assessment of risks in management systems and programs and in the development of goals and priorities for use by AIGA field units in developing their annual work plans and audit schedules;
- o Assist in the development of criteria and priorities that contribute to the total DOE audit effort involving financial management operations through liaison with management evaluation offices of the Department, certified public accountant (CPA) and independent public accountant (IPA) firms, State and local auditors, Defense Contract Audit Agency (DCAA) and other auditing components;
- o Review and coordinate revisions, as necessary, and develop recommendations for approval of the work plans of the AIGA field audit entities as they pertain to financial management matters;
- o Analyze financial management audit needs for the development of new or revised audit guidelines and strategies;
- o Assure coordination of planned financial management audits with audit staff of DOE contractors and management evaluation offices within the Department to avoid unnecessary duplication;
- o Review for policy adherence all audit reports on financial management subjects and develop recommendations for approval of reports pertaining to these matters;
- o Establish priorities and provide oversight for the audit of contracts by CPA and IPA firms, state and local auditors, DCAA, Department of Health and Human Services, internal audit organizations

of DOE and AIGA field entities that contribute to the Departmental audit effort;

- o Analyze procurement and grant audit needs for the development of new audit guidelines and strategies;
- o Review for policy adherence all reports on audits of the award, administration and management of contracts and grants, and develop recommendations for the final approval of reports concerning procurement operations in DOE entities;
- o Serve as the IG focal point for all activities relating to Departmental responsibilities under the Federal Managers' Financial Integrity Act (FMFIA);
- o Provide audit oversight for M&O audits and procurement audits; and
- o Serve as Contracting Officer's Representative (COR) for interagency audit agreements between the Department and both DCAA and the Department of Health and Human Services.

b. Performance Audits - The Director for Performance Audits provides the DAIG/AO, with the capability for planning, developing, and coordinating performance audits that provide insight into whether DOE programs are achieving the purposes for which they are authorized. This function includes conducting studies and assessments of DOE programs that are unusually susceptible to waste, fraud and abuse or that exhibit high levels of inefficiency in their practices, consulting with program directors and recommending (1) audit targets and priorities for use by the field offices in preparing their annual work plans and audit schedules; (2) providing the DAIG/AO with in-depth knowledge of Departmental programs and program management systems; (3) developing overall plans for and coordinating program audits which involve activities at many locations throughout the United States; and (4) providing liaison with GAO to avoid duplication of audit efforts involving Departmental programs. Specific functions are to:

- o Provide guidelines for audit policy implementation; ensure procedural consistency and uniform application of standards in DOE audit activities, including operations of contractors and grantees.
- o Develop plans for, coordinate and provide general guidance for the performance of multi-location reviews of the efficiency and economy of programs and operations of the Department.
- o Develop plans for and provide general guidance for the use of public accountants and other consultants to supplement the audit resources of the IG.
- o Review, evaluate and ensure progress of audits and expedite audits, as necessary. This includes establishing and operating a quality assurance function to ensure that IG audit reports meet mandated quality standards.

- o Review and coordinate revisions, as necessary, and recommend approval of the work plans of the AIGA field audit entities.
- o Analyze audit needs and provide input to AP³ for the development of new audit guidelines and strategies.
- o Maintain liaison with heads of headquarters organizations responsible for management systems and programs and with other concerned executive agencies.
- o Provide guidance, as necessary, to help Departmental accounting systems meeting standards established by the Comptroller General of the United States.

4. Regional Audit Offices. The three regional audit offices each direct financial and performance audits of the activities of the Department within their respective regions. In order to conduct these audits, CRO, ERO, and WRO each perform the following functions within their respective region:

- o Manage the total audit program for the region using a staff of auditors and personnel assigned to numerous field or site offices and mobile teams.
- o Perform tasks as assigned by the AIGA including development and analysis of audit techniques, strategies, policies, procedures and results, preparation of management reports, development of materials for use in responding to Freedom of Information requests, and preparation of materials for use in responding to congressional inquiries.
- o Monitor the efforts of Field Offices' Management Evaluations and M&O contractor internal audit staffs of over 100 persons to assure adequate reviews of their operations. Integrate the activities of these review groups into the overall audit plan for DOE.
- o Represent the AIGA in dealing with heads of DOE field organizations and large industrial contractors. On a local basis, represent the AIGA and maintain liaison with GAO, OMB, DCAA and various Federal, State and local officials and agencies.
- o Apply technical expertise and experiences as a member of agency or interagency panels, boards or committees concerned with audit policies and standards, organization of the audit function, or with audit programs of common interest. Provide expert advice to agency management concerning the audit of Departmental entities. Confer frequently with key officials at Headquarters and Departmental field locations concerning surveys and audits conducted under the regional supervision.
- o Produce reports that conform to Departmental and AIGA policy and adhere to requirements of the IG Act.
- o Execute annual audit statements with respect to the adequacy of the financial accounting and reporting systems of each M&O contractor

and certify annual financial statements of DOE revenue-producing organizations.

- o Maintain management support for the IG investigators in the region and assure appropriate coordination between the audit and investigative activities.

Regional audit offices also direct and monitor audits that are DOE-wide in scope. Regional audit office responsibilities for DOE-wide audits are to:

- o Report on audit results from DOE-wide audits. This function includes preparing reports that summarize the results of the multi-location audits and that make recommendations to high levels of management within the Department.
- o Direct and monitor all aspects of audits that are DOE-wide in scope, including performing surveys of programs, systems, functions or activity to determine where weaknesses or problems may exist.
- o Determine DOE locations that should be included in DOE-wide audits, and developing detailed audit guides for use by the various IG audit teams and other participating units in accomplishing the audits at the diverse DOE locations.

DEPARTMENT OF ENERGY

220000

* Deputy Secretary oversees Energy Programs and serves as Chief Operating Officer of the Department within the Office of the Secretary.

DEPARTMENT OF ENERGY FIELD RELATIONSHIPS

9/9/83

CHAPTER 3GENERAL AUDIT POLICIESA. SCOPE OF CHAPTER

This chapter addresses general audit policies that affect all audit work. It prescribes policies and procedures relating to the qualifications of the staff, the audit organization's and the individual auditor's independence, the exercise of due professional care in conducting the audit and in preparing related reports, and the presence of quality controls.

B. STAFF QUALIFICATIONS AND TRAINING

The Yellow Book requires that the staff assigned to conduct an audit should collectively possess adequate professional proficiency for the tasks required. Staff members conducting audits should possess

- o a knowledge of the methods and techniques applicable to government auditing and the education, skills, and experience to apply such knowledge to the audit being conducted;
- o a knowledge of government organizations, programs, activities, and functions;
- o the skills to communicate clearly and effectively, both orally and in writing; and
- o skills appropriate for the audit work being conducted.

It is OA policy that all auditors will comply with these training requirements. Detailed training policies and procedures are provided in Chapter 28.

C. INDEPENDENCE

It is AIGA policy that all staff, including contracted audit services, shall be free from personal and external impairments to independence, shall be organizationally independent, and shall maintain an independent attitude and appearance in all matters relating to audit work. Additional information on obtaining contractor assurance of independence is found on page 6-17.

1. Personal Impairments. The auditor is under a professional responsibility to maintain strict independence of judgment in planning and conducting audits and expressing opinions on financial statements. The auditor must not only be independent in fact, but must also appear independent to others. Circumstances in which OA staff members conducting reviews of DOE activities may have difficulty in remaining sufficiently objective to avoid conflicts of interest or the appearance of conflicts of interest include:

- o Personal or financial relationships that might cause the AIGA to limit the extent of review or disclosure;

- o Bias of attitude of such a nature or extent that impartial judgment is, or may appear to be, compromised;
- o Previous involvement, especially recent, in the management of the activity under review by the OA; and
- o Political or social convictions or loyalties.

The following procedures will be followed to ensure that auditors and supervisors are aware of potential conflicts of interest, to identify personal impairments, and to ensure that no audits are performed by auditors who have such impairments.

a. Conduct of Employees - All OA employees will be provided a copy of the standards of conduct applicable to DOE employees. These regulations are published as Title 10, Code of Federal Regulations (CFR), Part 1010. Also, employees must certify that they have received and read the handbook on Standards of Ethical Conduct for Employees of the Executive Branch that includes Part I of Executive Order 12674 and 5 CFR Part 2635.

b. Outside Employment - Employees are not prohibited from engaging in outside employment or activities unless such employment or activities would result in a conflict, or apparent conflict, of interest; involve the use of Government facilities, equipment, supplies, or employee duty time; cast a reasonable doubt about the objectivity of the employee's performance of official duties; impair the employee's mental or physical capacity or otherwise prevent the employee from devoting his or her primary interests, talents, and energies to the accomplishment of official Government duties; cause an employee to abuse leave privileges; reflect discredit of the U.S. or the Department; involve the use of official information not available to the public; involve employment of a sensitive nature for an enterprise which has or seeks business with the Department or an organization which is regulated by the Department or would be substantially affected by the employee's performance of official duties; or result in being paid by an outside enterprise for performing official duties for the Government.

All employees must seek advance approval from the AIGA through their Regional Manager or DAIG, as appropriate. Copies of approved requests shall be filed in the employee's official personnel file and forwarded to the Office of the Assistant General Counsel for General Law.

Senior Executive Service employees who intend to engage in outside employment must receive advance approval in writing from their reviewing official and the Office of the Assistant General Counsel for General Law.

For further information, employees should refer to 10 CFR 1010.

c. Financial Disclosure - All OA employees will cooperate in preparing and submitting required statements of employment and financial interests, and interests in energy concerns, as required by 10 CFR 1010.

d. Procurement Integrity - All auditors, supervisors, and managers will comply with the "Procurement Integrity" provisions of the Office of

Federal Procurement Policy Act Amendments of 1988 and their implementing regulations in the performance of requested preaward audits and in evaluating and selecting contracted audit services.

e. Supervisory Responsibilities - Managers and supervisors shall be alert for personal impairments of their staff. Potential impairments will be discussed with the staff and considered in staff assignments. If potential conflicts cannot be avoided in staff assignments, they will be called to the AIGA's attention.

f. Reporting Potential Impairments - Employees who become aware of the need to disqualify themselves from a particular matter in which they have been or may be assigned in the future, must seek the written approval, through the Regional Manager and the AIGA, of the Inspector General. (see OIG Directive IG-900A, "Personal Impairments to the Objectivity of Office of Inspector General Personnel", issued 6-24-88, for additional information.).

2. External Impairments. All auditors and supervisors are to be alert for external factors which could restrict audits or interfere with their ability to form independent and objective opinions and conclusions. Examples of these factors include the following:

- o Interference or influence external to OA that improperly or imprudently limits or modifies the scope of an audit.
- o Interference external to OA with the selection or application of audit procedures or in the selection of transactions to be examined.
- o Unreasonable restrictions on the time allowed to competently complete an audit.
- o Interference external to OA in the assignment, appointment, and promotion of audit personnel.
- o Restrictions on funds or other resources provided to OA that adversely affect its ability to carry out audit responsibilities.
- o Authority to overrule or to influence the auditor's judgment as to the appropriate content of an audit report.
- o Influences that jeopardize the auditor's continued employment for reasons other than competency or the need for audit services.

If these factors are identified at any time, auditors and supervisors are to follow these procedures:

a. Notify Supervisor - The existence of such a factor will be called to the attention of the next supervisory level, both within the OIG and the auditee, and attempts will be made to eliminate or compensate for the impairment.

b. Decline the Audit - If the impairment cannot be eliminated, the auditor and/or OA should decline to perform the audit.

c. Disclose Impairment - If an audit must be performed in spite of an identified impairment, that impairment shall be reported in the scope section of the audit report.

3. Organizational Independence. Chapter 2 describes OA's statutory authority under the IG Act and its organizational structure within the OIG and DOE. As such, OA's reporting level within DOE generally provides it with reasonable independence in performing audits and in reporting audit results. However, all auditors and supervisors are responsible for ensuring that OA's policies, procedures, and practices remain sufficiently comprehensive, suitably designed, adequately documented, and are carried out in a manner that continually protects it from any organizational impairments. If auditors or supervisors believe they have identified an organizational impairment, they should immediately notify the AIGA in writing.

D. DUE PROFESSIONAL CARE

This section sets forth general procedures to be followed by OA auditors to ensure that due professional care has been used in conducting audits and preparing related reports. Due professional care includes (1) considering the materiality and significance of matters being reviewed, (2) avoiding duplicate audit effort and, when possible, using the work of others, (3) follow-up on findings and recommendations from previous audits that relate to current audit objectives, (4) considering whether audit scope impairments have affected the audit, and (5) keeping supervisors informed of any other activities or events that could affect an audit.

1. Materiality and Significance. Auditors should consider materiality and/or significance in planning the audit and in selecting the methodology and designing audits tests and procedures as well as in deciding whether a matter requires disclosure in an audit report. Additional detail on this requirement is provided in chapter 5, section D, item 7.

2. Relying on Work of Others. It is AIGA policy to coordinate and cooperate with other federal, state, and local governmental auditors in auditing programs of common interest in order to reduce the amount of work required to accomplish audit objectives and to avoid duplicate audit efforts. In conducting an audit, auditors may rely on the work of others to the extent feasible once they satisfy themselves of the quality of the others' work by appropriate tests or by other acceptable methods.

a. Guidance - In determining whether to rely upon the work of others, the auditor should consider the following guidance.

(1) External Auditors. When the other auditors are external auditors, tests should include making inquiries into the professional reputation, qualifications, and independence of the auditors. The auditors should consider whether to (a) conduct additional tests and procedures such as reviewing the audit procedures followed and results of the audit conducted by the other auditors; (b) review the audit programs of the other auditors; and/or (c) review the working papers, including their understanding and assessment of internal controls, tests of compliance, and the conclusions

reached by the other auditors. The auditors may review the documentary evidence in the other auditors' working papers or make supplemental tests of the work conducted.

(2) Internal Auditors. When the other auditors are internal auditors, tests should include (a) determining whether they are qualified, (b) determining whether they are properly located in the organization in order to provide them with sufficient independence to conduct the audit objectively, (c) determining whether their work is acceptable by examining, on a test basis, the documentary evidence of the work conducted, and (d) conducting tests of the work. These tests may either (i) examine some of the transactions, balances, or work the internal auditors examined or (ii) examine similar transactions, balances, or work, but not those actually examined by internal auditors. Based upon this review, the auditors would decide what additional work, if any, would have to be done in order to accept the work of the internal auditors.

(3) Nonauditors. When relying upon the work of nonauditors (consultants, experts, specialists, etc., other than those hired to assist in the audit), the auditors should satisfy themselves as to the nonauditors' professional reputation, qualifications, and independence from the organization, program, activity, or function under audit. The auditors should also consider whether to (a) conduct additional tests and procedures such as reviewing the procedures followed and the results of the work conducted, (b) review the work program, (c) review the working papers, (d) make supplemental tests of the work conducted, and (e) consider the methods or assumptions used.

(4) Quality Control. The auditors should determine whether the above audit organizations have an appropriate internal quality control system in place and whether the organization participates in an external quality control review program.

b. Access to Working Papers - Auditors need access to the working papers of other auditors and nonauditors to satisfy certain of the above requirements. For working papers containing restricted information, the policies in chapter 7 should be followed. Arrangements need to be made to ensure that workpapers will be made available upon request to other government audit staffs and individual auditors. All contractual arrangements for government audits should provide for access to working papers.

c. Disclosure of Division of Responsibility - When auditors decide to rely on the work of others, but do not take full responsibility for that work, the auditors should indicate in the scope section of the audit report the division of responsibility between that portion of the work they conducted and that conducted by others, and the magnitude of the audit work completed by others. This guidance, however, does not preclude auditors from referring to others' work in their audit report even if the auditors did not verify it, if the work is used only for background or informational purposes and is not material or significant to the auditors' report. In these situations the auditors may just cite the information and its source in their audit report.

3. Audit Follow-Up. Management of the audited entity is primarily responsible for directing action and follow-up on recommendations. However, OA auditors should exercise due professional care in conducting audit work and

reporting results to ensure that they have reflected the results of prior audit work and have determined whether prompt and appropriate corrective actions have been taken by entity officials or other appropriate organizations.

a. Prior Audits - OA auditors should identify relevant prior audits and track the status of management's actions on significant or material findings and recommendations. Chapter 13 provides additional guidance on the Departmental Audit Report Tracking System (DARTS) and audit follow-up activities.

b. Open Recommendations - If significant or material findings and recommendations from prior audits that effect the current audit objective are identified, but remain uncorrected, this status will be disclosed in the current audit report.

4. Audit Scope Impairments. Audit scope impairments are factors external to the audit organization which can restrict the auditors' ability to render objective opinions and conclusions. Examples of these types of impairments are access to records problems or refusal by officials or employees of the auditee to meet with AIGA auditors. If AIGA auditors encounter these types of problems, they should be aware that, in accordance with the IG Act and DOE Order 2320.3A, "Office of Inspector General-- Responsibilities, Authorities, and Relationships with Other Departmental Elements," issued 5-18-92, the OIG is authorized to:

- o Have access to all records, reports, audits, reviews, documents, papers, recommendations, or other material available to the applicable Departmental elements which relate to programs and operations for which the IG has responsibilities under the Act.
- o Request such information or assistance as may be necessary for carrying out the duties and responsibilities provided by the Act from any Federal, State or local governmental agency or unit thereof.
- o Receive and investigate complaints or information from DOE employees concerning the possible existence of an activity constituting a violation of law, rules, or regulations, or mismanagement, gross waste of funds, abuse of authority or a substantial and specific danger to the public health and safety.
- o Require by subpoena the production of all information, documents, reports, answers, records, accounts, papers, and other data and documentary evidence necessary in the performance of functions assigned by the Act.

Although the OIG is not required to give advance notice or seek the approval of any official in DOE before conducting audits, auditors should attempt to keep the auditee's officials and employees informed of audit plans and to otherwise maintain positive working relationships to the extent possible. Accordingly, it is AIGA policy that auditors shall attempt to informally resolve access problems to the extent that it is possible to do so before resorting to more formal procedures.

a. Reporting Access Problems - In performing audits, auditors shall aggressively follow-up on all requests for records or information to ensure that it is obtained in a timely manner. When auditors do encounter access problems, they should (1) maintain a record of all discussions held and actions taken, and (2) promptly notify the AIGA through their Regional Managers. Regional Managers shall ensure that the AIGA is notified in writing within 10 days of the occurrence of an access problem.

b. Enforcement and Subpoena Authority - Although the IG can subpoena the production of various information and documentary evidence in the performance of his functions, this authority will normally be used only after appropriate consideration has been given to other means for obtaining the desired information or records. If auditors believe that this type of action is needed to further a legitimate audit, they should prepare a request in accordance with the guidance in OIG Directive IG-916, "Issuance of Inspector General Subpoenas," issued 6-24-86, and forward it through their Regional Manager to the AIGA for concurrence and further processing.

c. Access to Classified Information - IG personnel will maintain appropriate security clearances to access classified information or secure facilities. Prior to visiting a secure facility, IG staff will arrange for the submission of DOE Form DP-277, "Request for Visit or Access Approval," to the Office of Safeguards and Security (DP-34).

d. Management Representation Letters - A Management Representation Letter (MRL) is used to confirm oral statements made by an auditee during an audit to reduce the likelihood of misunderstandings between the auditors and the auditee. Refusal to sign such a letter could be considered a scope impairment in that the auditee is not being fully cooperative and open.

(1) Financial Statement Audits. In performing financial statement audits, auditors shall request and use MRLs in accordance with the AICPA standards.

(2) Preadward and Postaward Audits. Because the auditee already provides various and extensive signed representations to the contracting officer in the proposal document and later in the contract, MRLs are not to be requested or used for OIG preaward and postaward contract audits.

(3) Performance Audits. For performance audits, the Yellow Book states that auditors should, when they deem it useful, obtain from management written representations concerning the relevance and competence of evidence.

5. Keeping OIG Management Informed. The nature of work performed in the OIG often involves working in areas of high visibility or considerable interest to both internal and external sources. Events can and do occur in which the AIGA or the IG should be promptly informed so that higher-level management can be involved in decisions and to avoid sources of potential embarrassment to the OIG.

a. Potentially Significant Events - All auditors are responsible for keeping their Regional Managers and other supervisors informed of poten-

tial trouble areas or other issues involving high visibility within the Department. This includes particularly significant findings which have not yet been reported to the AIGA, access to records problems, potential legal proceedings, and inquiries by the media, GAO, members of the Congress, or other non-DOE parties. Regional Managers will determine which items should be brought to the AIGA's immediate attention.

(1) Weekly Activity Report. One method of calling items to the AIGA's attention is the Weekly Activity Report (see chapter 14 for further details on preparing this report).

(2) Illegal Activities. Responsibilities and procedures for informing the AIGA of indications of fraud and other illegal acts are discussed in chapter 4.

(3) Urgent Matters. For urgent matters, the AIGA should be promptly informed by telephone, facsimile, or electronic mail (E-Mail). It is the AIGA's responsibility for keeping the IG informed of appropriate matters.

(4) Written Memorandum. For selected matters, the AIGA should be informed by written memorandum. In particular, contacts with GAO and DCAA should be documented by memorandum and provided to the AIGA when substantive matters are discussed. Additional guidance for contacts with these organizations is provided in OIG Directive IG-914A, "Coordination with the Defense Contract Audit Agency," issued 2-11-88, and OIG Directive IG-915C, "Coordination with the General Accounting Office," issued 4-13-93.

b. Media Inquiries - It is OIG policy to respond to all media inquiries through the Special Assistant to the Associate Inspector General (SAAIG) to ensure consistency of approach, avoid duplication of effort, and prevent legal vulnerability. In accordance with OIG Directive IG-905B, "Media Inquiries," issued 1-22-90, the following procedures will apply for all contacts by the media:

(1) Referral to Special Assistant. If OA staff members at Headquarters or field offices are contacted by the media, they are not to provide any information at that time. Rather, they shall indicate that all media inquiries are to be directed to the SAAIG. The staff member shall then immediately advise the SAAIG, the AIGA, and their Regional Manager of the media contact.

(2) Comments Restricted. Once the OA staff member has referred the requester to the SAAIG and has advised management, the staff member has no further responsibility in this matter and should avoid further comment, except as directed by the SAAIG.

(3) Disclosure. OA staff members should be aware that there may be legal or policy reasons for withholding information from media representatives which could lead the SAAIG to disclose less than the full amount of information available. In particular, information will be released on ongoing investigations only with the specific approval of the AIGA and in accordance with OIG Directive IG-905B.

c. Congressional Inquiries - It is OIG policy to cooperate with Congress and to respond to congressional inquiries as fully as possible and in a timely fashion. All congressional inquiries, both oral and written, will be referred to and coordinated through the Counsel to the IG and in accordance with OIG Directive IG-906A, "Congressional Inquiries," issued 5-17-88.

d. Subpoenas or Depositions - OA employees or former employees may be requested to answer questions pertaining to information obtained or material developed or acquired during the course of official duties or because of the employee's official status with the DOE/OIG. Specifically, employees may be subpoenaed by courts or other authorities as witnesses to produce documents or to give testimony or depositions. However, in accordance with 10 CFR, Part 202, no DOE employee may answer a subpoena or other demand or give a deposition relating to information or material developed or acquired during the course of official duties or because of the employee's official status with the DOE/OIG without approval of the General Counsel, DOE. Therefore, any employee or former employee faced with such a request shall notify the IG, through channels, in accordance with OIG Directive IG-926A, "Notification of the Inspector General When Employees Are Subpoenaed or Ordered to Give Depositions," issued 7-13-89.

e. Requests for Confidentiality - Occasionally, auditors may receive information from individuals who request confidentiality. Auditors who encounter this situation should immediately discuss the matter with their supervisors. In discussing the information with officials outside of the OIG, auditors should exercise extreme care not to disclose the source of any confidential information received. In appropriate instances, such matters should be coordinated with the Office of Investigations.

E. QUALITY CONTROL/QUALITY ASSURANCE

All OA policies and procedures are intended to result in audits that are performed in accordance with internal quality control procedures. In addition, OA will participate in (1) periodic quality assurance reviews by the OIG's Quality Assurance Unit, and (2) reviews at least once every three years by an audit organization external to DOE.

1. Internal Quality Control System. This Manual, taken in total, is a compilation of policies and procedures that should result in high-quality audits and reports. However, procedures that are particularly important to this process include the following:

a. Supervisory Review - All audit work and related reports will be subject to adequate and timely supervisory review (see chapters 5, 6, and 12 for additional detail).

b. In-process Audit Surveillance and Review - AO will provide intensive in-process review for selected audits (see chapter 4, section C).

c. Technical Assistance - AO and AP³ will provide assistance, as appropriate, for audits utilizing computer-assisted or other advanced audit techniques (see chapter 8).

d. Report Referencing - All reports will be referenced prior to issuance of the official draft to ensure that they are supported by sufficient, competent, and relevant workpapers and have received appropriate supervisory review (see chapters 7 and 12 for additional detail).

e. Headquarters Post-Issuance Report Reviews - A post-issuance review of selected reports or group of reports not previously reviewed by AO will be performed as a means for maintaining and improving the quality of OA's audit reporting. A memorandum transmitting the results of these reviews will be forwarded to the appropriate Regional Manager.

f. Quality Assurance Reviews - All OA organizational elements will participate in the OIG's Quality Assurance Review Program (see below).

2. Quality Assurance Reviews. In addition to the quality control procedures identified above, it is AIGA policy that all OA organizational elements will be subject to review by (1) the OIG Quality Assurance Unit, and (2) by an external quality assurance review team.

a. OIG Quality Assurance Review Program - The policies and procedures for the OIG Quality Assurance Review Program are established in OIG Directive IG-103A, "Quality Assurance Review Program," 5-2-91. In accordance with this Directive, the AIGA will:

- o Provide input to the annual quality assurance plan.
- o Provide technical staff to assist in performing quality assurance reviews, as agreed to with the Director of the Quality Assurance Unit.
- o Provide comments on the team's findings and recommendations and respond in writing to the draft report.
- o Provide an implementation plan and quarterly status reports on the recommendations contained in quality assurance review reports. The status reports will continue until the recommendations have been implemented.
- o Implement quality control procedures for OA activities.

b. External Quality Assurance Reviews - At least once every three years, the OIG and/or AIGA will arrange for a quality assurance review by an OIG or other audit organization external to DOE.

CHAPTER 4GENERAL FIELD WORK POLICIESA. SCOPE OF CHAPTER

This chapter discusses the general policies that apply to all audit field work (both performance and financial audits) and briefly summarizes the material to be discussed in chapters 5 through 8.

B. SUPERVISION

Effective supervision is essential to the overall quality of an audit. Generally, higher-level supervisors can provide a broader perspective to help focus and sharpen audit objectives, select effective audit methodologies and reporting objectives, and determine the scope of work or resources that should be devoted to an audit in relation to other audit requirements and priorities. As an audit progresses, supervisory review can help the audit team to deal with unanticipated complications and to identify additional data needed to substantiate and refine audit findings. Exhibit A (A:AM04EXA.WPF) contains 7 supervisory principles to be used in managing staff.

1. Responsibilities. The AIGA and Regional Managers are ultimately responsible for all audit assignments and for ensuring that the staff receives appropriate guidance in performing its work. However, proper supervision is necessary throughout an assignment, with each level of staff involved in an audit having specific responsibilities for ensuring that audits are performed in accordance with prescribed AIGA standards and procedures. The various OA staffing levels and their respective responsibilities follow:

<u>Position</u>	<u>Responsibilities</u>
Auditor	Perform audit work in accordance with AIGA standards and procedures. Depending on experience, skills and job knowledge, will normally have responsibility for an audit segment or issue.
Auditor-in-Charge (AIC)	Ensure that an audit is performed in accordance with AIGA standards and procedures, to include preparing audit programs, workpaper support, and initial report drafts. Provide first level of review for work performed by assigned staff and contractors. A more detailed description of AIC responsibilities is found in exhibit B (A:AM04EXB.WPF) and in the <u>Handbook for Auditors-In-Charge: Leadership For Audit Excellence</u> (A:Hand-AIC.WPF).
Audit Director (AD)	Ensure that multiple or more complex audits are performed in accordance with AIGA standards and

procedures. Provide first level of review of audit programs, overall workpaper support, and tentative findings. A more detailed description of Audit Director responsibilities is found in exhibit C (A:AM04EXC.WPF).

Assistant Regional
Manager (ARM)

Provide supervision and professional leadership for all audit work in area of responsibility to ensure that AIGA standards and procedures are followed.

Regional Manager

Final responsibility for field office direction, supervision, and review of all audit work for which that office is responsible.

2. Timeliness of Supervision. Supervision is a continuing process. To be effective, it must be timely and include sufficient interim checks throughout the audit to ensure that work is properly planned, on schedule, and is being performed in accordance with plans. It requires auditors to keep their supervisors informed, and for supervisors to make such adjustments as are necessary to deal with changing or unanticipated circumstances. However, the proficiency and experience of the auditors and the difficulty of the audit assignment will affect the extent and timing of supervision required. To ensure that supervision is timely, OA supervisors and managers are responsible for:

- o Providing adequate guidance or direction throughout an audit, including suitable instructions to subordinates at the beginning of an audit and other work assignments commensurate with the abilities and experience of the assigned staff;
- o Approving audit programs in advance and ensuring that they are carried out and that audit objectives are met, unless deviations are justified and authorized in writing; and
- o Monitoring the status of work progress in a timely manner through periodic progress reports, status briefings, telephone calls, conference calls, site visits, and review of workpapers to ensure that audit work is being performed in accordance with prescribed standards and due professional care and that it adequately supports audit findings and conclusions.

3. Documentation of Supervision. Supervisors are responsible for ensuring that appropriate evidence of their supervision is documented and retained in the workpapers, in accordance with the procedures provided in chapter 7, section C. Points raised by a supervisor in reviewing audit programs and workpaper support shall be documented, addressed by the auditor, and subsequently cleared by the supervisor. Differences of opinion between an auditor and a supervisor concerning accounting and auditing issues will be documented and presented to higher-level supervisors to be resolved.

4. In-Process Audit Surveillance and Review. AO has responsibility for providing in-process review of selected audits on behalf of the AIGA. AO will

select and identify to the Regional Managers those audits which will be assigned to an AO monitor for close monitoring and review during the entire audit process. It will be the responsibility of AO to designate monitored jobs in the IG data base, and to notify the appropriate Audit Director of the designation. For the jobs so selected, the AO monitor will be involved in the major decisions involving the audit; will review and comment on the audit program and Go/No Go decisions; and will review and approve the tentative findings, draft report and final report within seven (7) working days of receipt.

C. FRAUD, ABUSE, AND ILLEGAL ACTS

Auditors are generally not responsible for conducting "investigations" of fraud, abuse or illegal acts. They are, however, required to be (1) aware of the characteristics and types of illegal expenditures and acts associated with the area being audited to be able to identify indications that these acts may have occurred, and (2) alert to situations or transactions that could be indicative of such acts. Auditors who note questionable activities requiring further investigation are responsible for (1) coordinating with the Office of Investigations, (2) notifying AIGA management, and (3) if necessary, adjusting the nature and scope of planned audit steps.

1. Coordinating with Office of Investigations. It is OIG policy that all OIG personnel having knowledge of possible criminal violations shall immediately refer this information to the AIGI, in accordance with OIG Directive IG-904A, "Coordination of Investigative Matters," issued 9-6-89.

a. Referrals - Regional Managers are authorized and encouraged to consult with and discuss referrals with the local senior investigators at the regional level. When a referral is made at the local (or higher) level, a memorandum entitled "Confirmation of Referral" shall be prepared and sent to the AIGA documenting the referral. This memorandum, not to exceed one page, should describe (1) how the referral came about (the source of the information), (2) the characteristics that led the auditor to pursue the potential illegal act, (3) the regulation or other criteria believed to be violated, and (4) the name and telephone number of the auditor most familiar with the referral. The memorandum request notification of the OA contact if an investigation is opened.

b. Continuation of Audit - The AIGA, in consultation with the AIGI, shall decide whether continuation of the audit will interfere with or compromise an investigation. Audit work shall not be delayed or discontinued without the AIGA's explicit approval.

c. Release of Information - All OA staff are cautioned that, if they do become aware of a pending or on-going investigation, they are not to reveal the existence of, discuss with non-OIG personnel, or to otherwise release information about the investigation without the prior consent of the AIGA.

d. Workpapers - Auditors should cooperate fully with OIG investigators. This includes allowing OIG investigators to examine audit workpapers.

e. Coordination - Additional requirements for coordinating with the Office of Investigations are found in chapters 5 and 6.

2. Informing AIGA Management. Whenever indications of fraud or other illegal acts are disclosed during an audit, auditors should immediately inform their immediate supervisor and the Regional Manager. The Regional Manager is responsible for notifying the AIGA and/or the DAIG/AO.

a. The AIC is responsible for documenting any indications of potential criminal violations and other types of illegal conduct. As a minimum, the documentation should describe the statute, regulation, etc., believed to be violated and the questionable activities or indications of illegal acts. If the questionable activities were discussed with Office of Investigation personnel at the local level, the "Confirmation of Referral" should satisfy this requirement. Otherwise, a Memorandum of Referral to the AIGA should be prepared. In either case, the memorandum will be sent to the AIGA through the Regional Manager and DAIG/AO.

b. A copy of the documentation prepared, including any memorandum of referral or confirmation of referral, should be retained in a job file and/or the workpapers in case later reference is made to the referral in an audit report.

c. The DAIG/AO will ensure that any memorandum of referral or confirmation of referral sent to the AIGA is forwarded to the AIGI.

3. Adjusting Scope of Audit Steps. If information of possible abuse or illegal acts comes to an audit team's attention, the team is responsible for considering the potential impact of these acts on audit results. If audit results could be significantly affected, the audit team may need to extend the audit steps and procedures, as necessary, to determine whether the acts occurred, and if so, to determine the extent to which audit results were affected. However, major adjustments in scope may not be necessary if the audit team has properly planned an audit and included steps to evaluate compliance with laws and regulations, and detect and report significant illegal acts and abuses (see chapter 5 for additional planning guidance).

a. For financial audits, auditors must do sufficient testing to ensure that possible illegal acts do not have a material effect, either directly or indirectly, on the financial statements or results of financial related audits. For both financial and performance audits, the extent of additional testing requires judgment and experience in order to perform sufficient steps to detect major noncompliance without spending an unreasonable amount of resources on those steps.

b. Although auditors need to exercise due professional care and caution in pursuing indications of illegal acts so as not to interfere with potential future investigations or legal proceedings, the belief that auditors can easily jeopardize a legal case by aggressively pursuing indications of illegal acts lacks foundation. More frequently, auditors do not go far enough with their testing. Early coordination with the Office of Investigations is a key to assuring a careful and successful examination of potentially illegal acts.

4. Reporting Illegal Acts. When illegal or potentially illegal acts are identified, auditors should follow the guidance in chapter 9 for specific reporting policies and procedures.

D. OTHER FIELD WORK REQUIREMENTS

Detailed field work requirements are provided in the following chapters:

1. Planning. Planning is the first fieldwork standard for both financial and performance audits. Work must be adequately planned in order for AIGA audits to meet their objectives. Chapter 5 deals with the major types of planning undertaken by OA, including workload planning to assure adequate audit coverage and efficient use of resources, procedures for identifying audit ideas and needs, and general planning considerations to assure consistency and quality among all AIGA audits.

2. Conducting the Audit. Chapter 6 provides detailed guidance for various stages of field work, from initiating the audit via audit profiles and assigning supervisory responsibilities to executing the survey and verification steps. As illustrated in exhibits A, B, and C, these stages generally account for the majority of time spent on an audit.

3. Workpaper Support. Workpapers form the critical link between field work and the audit report. They are necessary to provide a systematic record of work performed, to assist staff members in pulling ideas together for reporting, and to provide a record of information and evidence supporting the findings, conclusions, and recommendations contained in a report. In a very real sense, workpapers are the backbone for all AIGA work. Accordingly, the AIGA has adopted very specific standards for workpaper support. These standards are detailed in chapter 7.

4. Advanced Audit Techniques. In today's computer age, auditors must be able to (1) audit organizations where ADP or computer operations are an integral part of the operations being evaluated, and (2) use computer assisted or other advanced audit techniques to collect and analyze audit evidence. Chapter 8 discusses auditing in an ADP environment and various advanced audit techniques, including standardized data collection, and statistical sampling.

SUPERVISORY PRINCIPLES FOR MANAGING STAFF

1. Establish high goals and expectations.
 - a. Set high goals and expectations for your staff and yourself.
2. Assign as much responsibility as the employee can handle, or is willing to accept.
 - a. Give the staff as much responsibility as you think they can reasonably handle. Inexperience does not equate to inability.
3. Give credit for outstanding accomplishments.
 - a. Recognize excellent work and encourage staff to work as a team.
4. Be honest.
 - a. Keep the staff informed. Honesty is the best policy.
 - b. Review work promptly to catch mistakes before they are repeated.
 - c. Explain the reason for doing things.
5. Stress teamwork.
 - a. Ask for the staff's input and opinions on projects.
 - b. Give the staff the chance to present their findings to upper management and the auditee. Be there to back them up if necessary.
6. Use as much of the employee's work as possible (do not over-correct).
 - a. Avoid unnecessary over-corrections. Try to work with what the staff have done instead of starting over.
7. Remember that every employee is different and valuable.
 - a. Maintain an open door policy. Be open to questions or ideas.
 - b. Demonstrate concern for the staff's career development by encouraging certification and continuing education.
 - c. Assign to each new staff member a sponsor who has similar interests and background.
 - d. Rotate team assignments to allow a variety of experiences.
 - e. Have patience.

AUDITOR-IN-CHARGE (AIC) ROLES AND RESPONSIBILITIES

An auditor-in-charge (AIC) is responsible for directing a specific audit. The AIC must be able to direct the audit through its various phases--i.e., survey, verification, and reporting--in an expeditious and sound manner and ensure that established policies, procedures and professional audit standards are effectively applied. Normally, an AIC will be assigned to an audit for its full duration, regardless of other staffing adjustments that may be made, and is expected to become the single most knowledgeable individual on the audit. An AIC's responsibilities include the following:

1. Working Relationships. AICs will take the lead on an assignment in terms of keeping management informed, coordinating audit activities, and maintaining effective working relationships.
 - a. Keep Management Informed. AICs will keep supervisors and other OIG management informed of potentially significant events, trouble areas, high visibility issues, access to records problems, potential legal proceedings or illegal acts, and inquiries by the media, GAO, members of the Congress, etc.
 - b. Personnel and Administration. AICs will follow established DOE and OIG procedures for personnel administration, work force discipline, employment policies, time and attendance, leave administration, and travel.
 - c. Audit Coordination. As necessary, AICs will coordinate their audit efforts within the Office of Audits (OA), with the internal audit staff of the audit entity, and with other audit organizations (e.g., GAO, DCAA, other OIGs, and State or local auditors).
 - d. Coordination with Investigations. AICs will coordinate their audit efforts with OIG Investigations. Specific requirements follow:
 - (1) When initiating audit work, the AIC are to meet with Investigations to obtain any investigative information that could help in developing audit findings and to ensure that the audit will not interfere with an ongoing investigation.
 - (2) AICs will notify Investigations, through their supervisory chain, if indications of fraud or other illegal acts are disclosed during an audit.
 - (3) Prior to issuing a TF&R, the AIC will contact Investigations to ensure that release of findings will not interfere with an ongoing investigation.
 - e. Keep Staff Informed. In addition to providing information "up-the-chain," AICs must also work to ensure effective communication with their employees.
2. Supervision. AICs will supervise audit activities to ensure that they are performed in accordance with AIGA standards and procedures. Specifically, they will:

- a. Ensure that staff are assigned tasks commensurate to their abilities and are utilized in a productive manner;
 - b. Work with staff to identify specific needs and to develop needed skills and abilities;
 - c. Provide the first level of review for work performed by assigned staff, to include reviewing all workpapers they prepare;
 - d. Provide "on-the-job training" (OJT) to trainees, prepare OJT accomplishment records, and assist in evaluating trainee performance; and
 - e. Ensure that appropriate evidence of their supervision, as well as that of their supervisors, is documented and retained in the workpapers.
3. Planning. AICs are responsible for planning a specific audit, to include establishing how audit objectives can be met while making optimum use of limited audit resources. The plans for an audit will be reflected in audit programs for survey and verification work that comply with audit standards and policies and are consistent with approved audit objectives.
- a. Audit Objectives. The AIC will address audit objectives, scope, and methodology in the audit program, and ensure that the scope of work and methodology (i.e., audit techniques to be used) are consistent with the audit objectives.
 - b. Laws and Regulations. Consistent with audit objectives, the AIC will design audit steps in order to assess compliance with relevant laws and regulations and to provide reasonable assurance of detecting fraud, abuse or other illegal acts.
 - c. Internal Controls Testing. The AIC is required to design audit steps to test compliance with internal control objectives and to document their understanding of the internal control structure.
 - d. Transaction Testing. The AIC will normally design transaction tests to determine the significance or extent of problems. Also, in planning audit steps at M&O contractors, the AIC should consider testing done by other auditors, especially that conducted by internal auditors as part of the required 5-year audit cycle.
 - e. Testing for Data Reliability. AICs will (1) determine the level of review and testing needed to ensure the reliability of computer processed data to be used in an audit and (2) coordinate these plans with AP³ and AO.
 - f. Audit Follow-up. An AIC is required to identify reviews or audits that cover the same or related subject matter as their assigned audit.
4. Initiating An Audit. AICs will ensure that audits are properly authorized and that the auditee is kept informed of audit objectives and scope

of planned work.

- a. Letter of Notification. AICs will prepare Letters of Notification that appropriately state audit objectives and scope of planned work.
 - b. Entrance Conference. AICs will attend the entrance conference on their assigned audit and record the results of the meeting.
 - c. "Kick-Off" Meetings. AICs will arrange for "kick-off" meetings at subordinate levels of an audit entity before initiating audit work.
5. Survey Work. Within the framework of the survey program, the AIC is responsible for gathering data, identifying potential findings, and determining the nature and scope of audit work that would be needed to verify the findings. At the end of the survey, AICs will prepare an End of Survey Decision Contract (EOSDC), recommend a Go or No Go decision, and submit to OIG management for review.
6. Conducting Verification Work. The AIC will ensure that such information as necessary to accomplish audit objectives is collected, analyzed, interpreted, and documented during verification work. The AIC will translate planned audit steps into tasks or work segments that can be assigned to and carried out by individual staff members. If the audit does not appear to be resulting in reportable findings, AICs must use their own initiative in assessing the effectiveness of audit steps and results of their work and making or recommending adjustments.
- a. Revised Audit Objectives. Following any survey work, the AIC is responsible for ensuring that any revisions to the audit objectives are reflected in the audit program, and that the auditee is duly informed of any redirection in the audit.
 - b. Audit Evidence/Techniques. AICs will ensure that appropriate techniques are used in obtaining and documenting audit evidence, and in analyzing and summarizing this evidence.
 - (1) Data from Computer-Based Systems. AICs will ensure that a reliability assessment is made when computer-generated data or information is (1) an integral part of the auditee's operations being audited, or (2) to be used in a report or in support of a finding.
 - (2) Data Collection and Sampling Techniques. AICs will follow appropriate DOE approval procedures when using questionnaires and structured interview forms. They will also utilize appropriate sampling techniques and ensure that any conclusions and generalizations made are valid, with particular attention paid to (1) the basis for sample selection, (2) size of audit universe, (3) attributes of the sample (error rates, sample interval, confidence levels, etc.), (4) results of the sample, and (5) basis for projecting sample results.
 - (3) Illegal Acts. The AIC is responsible for documenting any indication of potential criminal violations and other types of

illegal conduct.

- (4) Internal Controls. The AIC is required to document in the workpapers the results of any required assessment of internal controls.
 - c. Workpapers. AICs will ensure that workpapers on each audit are prepared and maintained in accordance with AIGA standards.
 - (1) Workpaper Preparation. AICs will ensure that the results of all audit work is carefully recorded and documented in the workpapers in accordance with AIGA policies.
 - (2) Security. AICs will ensure that workpapers are properly safeguarded and any classified information obtained is handled, controlled, stored and mailed in accordance with DOE requirements;
 - d. Tentative Findings and Recommendations (TF&R). AICs will prepare TF&R's, to include the Estimated Monetary Impact form, to ensure that findings are fully developed and that claimed savings are carefully documented. Tentative findings will be informally staffed with the auditee to verify factual accuracy.
7. Reporting Audit Results. AICs will ensure that all audit results for their assignments are reported in accordance with AIGA reporting policies.
- a. Official Draft. AICs will prepare official drafts that reflect management comments and are written in accordance with prescribed reporting policies and formats.
 - b. Referencing. The AIC will ensure that a report is properly cross-indexed and prepared for referencing.
 - c. Exit Conference. AICs will attend the exit conference for their assigned audit and record the results of the meeting.
 - d. Final Report. AICs will prepare final reports in accordance with OA and OIG reporting policies.
8. Administrative/Other Duties As Assigned. AICs are to ensure compliance with various administrative and personnel requirements and to perform other duties as assigned.
- a. Action Items. Consistent with their assigned audits, AICs may be asked to help process action items, such as short suspense requirements, on behalf of their region or audit headquarters.
 - b. IGDBMS Input. AICs will periodically enter information in the IGDBMS to ensure that job status, milestones, time charges, and comments are correct. Chapter 6 discusses the AICs IGDBMS responsibilities in more detail.

- c. Identifying Audit Ideas. AICs will be alert to identifying audit ideas for subsequent audits, and will submit audit lead sheets or profiles whenever they spot potential audit issues.

AUDIT DIRECTOR ROLES AND RESPONSIBILITIES

Audit Directors (ADs) manage and direct audit operations at various work sites located in the three regional audit offices. They provide supervision and professional leadership to a staff of auditors conducting financial and performance audits of DOE activities, programs, and organizations. As the senior OIG representative at an audit site, ADs are in a unique position to "set the tone" for how the Office of Audits (OA) is perceived by its employees, auditees, and the public. As such, ADs must be especially diligent in ensuring that activities under their control are managed in accordance with applicable requirements and in an effective and efficient manner.

ADs are the primary source of OIG institutional knowledge for activities within their assigned audit area. They must thoroughly understand the mission, function, and reporting relationship of each audit entity, as well as the role these entities play in the Department's overall mission and how they relate to other DOE operations. They must understand how each entity is affected by internal and external forces, changing Departmental goals and objectives, and budget and programmatic trends. They must also have (1) a sense of how the local community relates to DOE, including the realities and impact of public opinion and local or state political processes on DOE operations; (2) a sense of priorities in terms of which operating elements of an entity are most important at a given point in time; (3) a "vision" as to the future of DOE operations; and (4) a continuing awareness of the operating environment in which the entities function and of other conditions relevant to the audit process.

The following sections provide more detail regarding an AD's responsibilities for (1) general management activities, (2) directing specific assignments, (3) developing functional or technical expertise consistent with assigned audit areas, and (4) handling various administrative duties on behalf of the OIG.

GENERAL MANAGEMENT ACTIVITIES

ADs are responsible for the overall management of activities at an audit site. Specific requirements include the following:

1. Keeping Management Informed. ADs are to keep OIG management informed of potentially significant events, trouble areas, high visibility issues, access to records problems, potential legal proceedings or illegal acts, and inquiries by the media, GAO, members of the Congress, etc. Specific requirements include:
 - a. Preparing weekly activity reports;
 - b. Referring media inquiries to Headquarters;
 - c. Arranging for and/or participating in audit director meetings and visits by management;
 - d. Briefing OIG management on issues as requested; and
 - e. Informing OIG management if indications of fraud or other illegal acts are disclosed during an audit.

2. Staff Supervision. As the senior supervisor at a site, ADs will ensure that audit and secretarial staff perform assigned duties in accordance with AIGA standards and procedures. Specifically, they will:
 - a. Ensure that audit and secretarial staff are assigned tasks commensurate to their abilities, are productively utilized, and perform their assigned tasks in an appropriate and professional manner;
 - b. Ensure that staff have up-to-date Audit Manuals and OIG directives;
 - c. Provide the first level of review of audit programs, overall workpaper support, and tentative findings;
 - d. Review all workpapers prepared by auditors-in-charge (AICs) and selectively review workpapers prepared by staff assistants; and
 - e. Be alert to personal impairments of their staff.
3. Coordination/Liaison. ADs will maintain liaison with various organizations for work involving their assigned audit area. This includes:
 - a. Periodically meeting with Departmental and contractor officials to discuss OIG audits and other issues;
 - b. Establishing a direct relationship with internal auditors at the Management and Operating (M&O) contractors [However, any instructions to the internal auditors will be issued through the appropriate contracting officers];
 - c. Coordinating audit coverage in their audit area with external audit groups--e.g., GAO, DCAA, other OIGs, and State or local auditors;
 - d. Coordinating audit work required at other locations with the affected regions and keeping regional managers apprised of all interregional audit activity; and
 - e. Ensuring that audit work under their control is coordinated with the Regional Inspector General for Investigations (RIGI) or the Resident Agent in Charge (RAIC) to (1) determine whether investigative information would help in developing audit findings and (2) ensure that audit work or release of findings will not interfere with an ongoing investigation.
4. Security. ADs have overall responsibility for security at an audit site, to include ensuring that:
 - a. All local security requirements are followed;
 - b. Classified information is handled, controlled, stored and mailed in accordance with DOE requirements;
 - c. Workpapers, equipment, and facilities are provided adequate security and safeguards; and

- d. Requests for security clearances are submitted in a timely manner.
5. Training and Development. ADs will take a proactive role in the training and development of their staff.
 - a. ADs will work with staff, particularly AICs, to identify specific needs and to develop needed skills and abilities.
 - b. ADs will review employee training needs; prepare annual training requirements; review, approve and ensure timely submission of training requests; and complete employee training evaluation forms.
 - c. ADs will ensure adequate oversight and training for trainees, to include reviewing "on-the-job" (OJT) accomplishment records, periodically evaluating their performance, discussing their career progress, and providing any necessary counseling.
6. Keep Staff Informed. In addition to providing information "up-the-chain," ADs must also work to ensure effective communication with their staff.

DIRECT SPECIFIC ASSIGNMENTS

ADs will supervise, direct, or otherwise monitor all audits within their assigned audit area. In carrying out this function, ADs will control and schedule all jobs under their supervision. They will either perform the required tasks or assign duties to AICs and other staff with due regard for job requirements and staff capabilities. Where AICs are assigned responsibility for an audit, ADs will ensure that they (1) are informed of their expected duties [see separate description of AIC roles and responsibilities], (2) perform such duties in an appropriate manner, and (3) are not assigned other duties that would conflict with successful completion of the audit. If audit work is performed by contract auditors, ADs will ensure that it is conducted in accordance with contract terms and other requirements.

1. Audit Profiles. ADs will prepare or review Planned Audit Profiles.
2. Letter of Notification. ADs will ensure that Letters of Notification appropriately state the purpose of the audit and scope of planned work.
3. Assign Staff. As delegated by regional management, ADs will ensure that an adequate number of staff with appropriate experience, skills and knowledge for the job are assigned to each audit.
4. Survey Program. ADs will review and approve survey programs to ensure that the nature and scope of work planned is consistent with audit objectives.
5. IGDBMS Input. ADs will periodically review information in the IGDBMS to ensure that job status, milestones and comments are correct.
6. Entrance Conference. ADs will attend entrance conferences that affect their assigned audit area.

7. Site Visits. If audits involve work at other sites, ADs will periodically conduct site visits in order to discuss audit progress and, as appropriate, to offer direction.
8. End of Survey Decision Contract (EOSDC). ADs will review the EOSDC, indicate their concurrence with the proposed Go/No Go decision, and submit to regional management for further review.
9. Audit Program. ADs will review and approve audit programs for verification work to ensure that the planned scope of work and audit steps are consistent with approved audit objectives and the EOSDC.
10. Tentative Findings and Recommendations (TF&R). ADs will review TF&R's, to include the Estimated Monetary Impact form, to ensure that findings are fully developed and that claimed savings are carefully documented.
11. Referencing. ADs will ensure that proposed official drafts are referenced pursuant to AIGA-prescribed procedures.
12. Official Draft. ADs will ensure that official drafts reflect management comments and are written in accordance with AIGA reporting policies.
13. Exit Conference. ADs will attend exit conferences that affect their assigned audit area.
14. Final Report. ADs will review reports prior to issuance for quality, consistency, and compliance with OA and OIG reporting policies.
15. Fact Sheet. ADs will prepare Fact Sheets to ensure that the narrative accurately summarizes the monetary or programmatic impact of the audit.
16. Departmental Position. ADs will review Departmental Positions to ensure that they are consistent with audit findings and recommendations.

FUNCTIONAL/TECHNICAL EXPERTISE

ADs are to work towards developing an audit team that has sufficient functional or technical expertise to effectively audit all audit entities or activities within their assigned areas. They will "coach" or otherwise provide guidance, technical direction, and professional leadership for their staff. Specific requirements follow:

1. Current Files. ADs will maintain files on each audit being performed by their office in accordance with AIGA standards.
2. Permanent Files. ADs will develop, maintain, and periodically update permanent files on organizations or activities within their assigned areas, to include information on legislation, budgets, organizational descriptions, prior audit reports, DOE directives, and such other information as will assist them in reviewing assigned audits and future workload planning.
3. General Planning/Audit Guidance. ADs will help evaluate audit ideas and

develop audit goals, plans, and guidance for their assigned audit areas.

- a. Audit Profiles. ADs are to submit audit lead sheets/profiles whenever they spot potential audit issues.
 - b. Annual Planning and Budgeting. ADs will submit information for their assigned audit areas, such as total auditable dollars, to help develop audit work plans and budgets. If ADs become aware of audit requests or referrals, these will also be directed to regional management.
 - c. Audit Guidelines and Strategies. ADs will assist regional management in analyzing audit needs and providing input for the development of new audit guidelines and strategies.
4. Internal Control Assessments. ADs play a central role in helping the OIG meet its responsibilities for annual assessments of the internal controls maintained by DOE and its M&O contractors.
- a. Integrated Contractor Audits. ADs will track the status of audits performed of the integrated contractors by their internal auditors.
 - b. FMFIA. ADs will assist in the annual reviews required by the Federal Managers' Financial Integrity Act (FMFIA).
 - c. Certify Annual Audit Statements. ADs will sign VANEAs and return them to the respective Field Elements by March 1 for the previous fiscal year.
5. Action Items. Consistent with their assigned audit areas, ADs may be asked to help process action items, such as short suspense requirements, on behalf of their region or audit headquarters.
6. ADP/Advanced Audit Techniques. In accordance with the Audit Manual, audit work involving ADP and other advanced audit techniques is to be coordinated in advance with AP³ and AO.
- a. Data from Computer-Based Systems. ADs will assist their staff in (1) determining the level of review and testing needed to ensure the reliability of computer-processed data to be used in an audit and (2) coordinating these plans with AP³ and AO.
 - b. Standardized Data Collection Techniques. ADs are to be aware of DOE approval procedures for use of questionnaires and structured interview forms.
 - c. Sampling Techniques. For audits involving statistical sampling, ADs will ensure that appropriate sampling techniques are used and that any conclusions and generalizations made are valid. Particular attention will be paid to (1) the basis for sample selection, (2) size of audit universe, (3) attributes of the sample (error rates, sample interval, confidence levels, etc.), (4) results of the sample, and (5) basis for projecting sample results.

7. Use of Experts and Consultants. If the regional audit staff does not have needed specialized training or skills, ADs are responsible for requesting the use of appropriate experts and consultants.

ADMINISTRATIVE

ADs are to ensure compliance with various administrative and personnel requirements.

1. Personnel. ADs are to follow established DOE and OIG procedures for personnel administration, work force discipline, and employment policies.
 - a. Performance Appraisals. ADs will follow established DOE and OIG performance appraisal procedures. Specifically, they will:
 - Review standards and elements with employees;
 - Oversee and document employees' performance throughout the rating period;
 - Perform and discuss interim appraisal with the employee;
 - Perform, document, and discuss annual appraisal;
 - Approve within grade increases; .
 - Recommend awards; and
 - Counsel employees with performance problems.
 - b. Recruitment/Promotions. ADs will participate in hiring or promoting employees, with due regard for DOE and OIG policies on affirmative action and upward mobility. Their duties include
 - "Spreading the word" on openings;
 - Interviewing candidates for positions; and
 - Serving on selection panels or otherwise recommending applicants to be selected, promoted, or reassigned.
 - c. Discipline/Compliance with Rules. ADs will follow prescribed procedures for maintaining work force discipline and compliance with other requirements. Specifically, they will:
 - Keep employees informed of rules, regulations, and standards of conduct, and maintain order and discipline within the framework of established procedures;
 - Ensure employee compliance with local policies, such as parking, smoking, and reporting for work during hazardous weather;
 - Ensure that assigned staff comply with requirements for

seeking advance approval for outside employment, submitting financial disclosure statements, etc.;

- Gather, analyze, and consider carefully all facts and circumstances before taking or recommending corrective action; and
- Issue oral admonishments, notices of reprimand, and initiate proposed actions after consultation with regional management and the OIG Personnel Officer;

2. Payroll/Time and Attendance. ADs will follow established DOE and OIG procedures for recording time and attendance and certifying payroll documents. Specifically, they will:
 - a. Review and approve time and attendance reports;
 - b. Certify payroll input to Headquarters; and
 - c. Ensure that time is entered into IGDBMS on a timely basis and that it is consistent with time charges submitted on time and attendance reports.
3. Leave Administration. ADs will follow established DOE and OIG procedures for leave administration, including scheduling annual leave with due regard for workload demand and employee needs. Specifically, they will:
 - a. Approve annual, sick, administrative, and other leave;
 - b. Review and approve requests for advance leave or leave without pay;
 - c. Counsel employees on leave abuse; and
 - d. Ensure that leave usage is adequately documented and recorded.
4. Travel. ADs will ensure that they and their assigned staff follow established DOE and OIG travel procedures. Specifically, they will:
 - a. Review and approve travel orders and travel vouchers;
 - b. Budget for travel needs; and
 - c. Keep their region and Headquarters informed of interregional travel and travel not directly related to a specific audit.
5. Facility/Office Management. ADs will serve as the local OIG representative in establishing reasonable working conditions and local office policies. Specifically, they should:
 - a. Ensure adequate space, facilities, equipment, and supplies for their staff;
 - b. Ensure accuracy of computer inventory (ADP equipment);

- c. Oversees office management, such as mail, telephone, etc.;
- d. Review employee toll calls;
- e. Arrange for employee participation in programs such as health screening and security and environmental briefings; and
- f. Ensure that an office filing system is established and that an inventory of professional literature is obtained.

CHAPTER 5PLANNINGA. SCOPE OF CHAPTER

Planning is an important fieldwork standard for both financial and performance audits. Work must be adequately planned in order for OA audits to meet their objectives. This chapter deals with the general planning needed in order for the AIGA to assure adequate audit coverage and efficient use of resources and consistency and quality among all OA audits.

B. WORKLOAD PLANNING

OA is continually revising its goals--and its plans for achieving those goals--based on an ever-changing audit environment. The primary vehicle used for this type of planning is the annual work plan cycle, as influenced by long-term planning mechanisms or factors.

1. Long-Term Planning Mechanisms. The audit planning process is primarily driven by budget and program policy issues. These issues are regularly addressed as part of the annual work plan cycle. However, this process is conducted within the context of long-term planning mechanisms, such as (1) the identification and development of major issue areas, (2) OA's goals and objectives, and (3) long-term audit cycles.

a. Major Issue Areas - OA continually identifies and develops major issue areas in which it attempts to provide reasonably comprehensive audit coverage. The following six key areas are currently the focus of our audit efforts:

- Contract Administration
- Program Management
- Infrastructure
- Financial Management
- Deterrents
- Expansion of Laboratory Missions

b. Goals and Objectives - AP³ is responsible for developing goals and objectives with input from all OA organizations. These goals and objectives lay out a broad framework within which OA can evaluate the economy, efficiency, and effectiveness of DOE programs and operations, emphasize work in the major issue areas; detect and deter fraud and abuse by ensuring proper internal controls are established and maintained; and identify, obtain, and administer sufficient AIGA resources to carry out an efficient and effective Inspector General program of audits with special emphasis on equal employment opportunity.

c. Risk Assessments - Because of resource limitations, OA recognizes that not all functions or activities in the Department can be audited every year or covered in each audit. Therefore, OA attempts to ensure audit coverage of major risk areas. For example, with respect to the Department's

integrated contractors, OA has established the policy that audits of contractor's operations will be based upon a risk assessment to provide an acceptable risk ranking methodology for determining the frequency of audit.

2. Annual Planning and Budgeting. AP³ is responsible for developing and implementing the audit resource planning and budgeting process and for providing associated staff services. The Regional Managers, along with the DAIG/OA, are responsible for submitting necessary information for their respective offices and areas of responsibility to help develop audit work plans and budgets.

OMB Circular A-73 requires each agency to prepare an audit work plan at least annually and to adjust it as necessary to provide for unforeseen priorities. The Department stipulates that an annual integrated audit work plan will be developed in accordance with DOE Order 2321.1B, "Auditing of Programs and Operations," dated 5-14-92. The OIG, as an integral part of the Department, must also prepare and submit an annual budget.

The following procedures are a necessary part of the process to produce information essential to comply with these audit work planning and budgeting requirements.

a. Annual Resource Estimate - AP³ is responsible for estimating staffing resource needs for future years. This process generally follows the schedule below:

<u>Timeframe</u>	<u>Activity</u>	<u>Responsibility</u>
10/01-11/10	Long-range goals & objectives derived.	AP ³
	Categories of auditable entities and decision rules (governing resource allocation) established.	OA Managers AP ³
11/10-12/30	Staffing level computation (using decision rules).	AP ³
	Amount of unaudited Departmental expenditures estimated.	AP ³

b. Annual Budget - AP³ is responsible for gathering together the necessary annual budget information for AIGA requirements to be incorporated into the OIG's overall budget request. This phase should be started by January 1 and targeted for completion by April 15. (The budgeting process, however, is significantly influenced by factors outside the control of OA, and may be more realistically viewed as continuous.) Managers will be notified during this time of the information they are required to submit. The information accumulated through the Annual Resource Estimate is an integral part of this budget information. DOE officials who rely on the OIG for audit services are requested in January to estimate their audit needs in the next fiscal year. Examples of these services are cost-incurred audits, preaward audits, financial certification audits, and other similar reviews.

c. Annual Program Guidance - Program guidance is provided as a basis for developing the annual audit work plan. Preparation of the guidance will commence on March 15, and be completed by April 30. The guidance sets priorities for AIGA audit coverage of important DOE issues and operations by establishing audit priorities and provides the basis for assigning AIGA resources. This guidance also covers annual budget assumptions, submission dates and formats, and overall coordination to avoid duplications and to maximize audit coverage within DOE. Program guidance will also be provided to the field offices and other equivalent DOE offices for their management evaluation staffs and M&O contractor audit staffs under their jurisdiction. The guidance is based on the current budget request, financial trend data, and the current audit environment.

d. Annual Audit Work Plan - The OIG's audit work plan focuses the DOE's audit resources on those program priorities outlined in the program guidance. Work on the plan will commence on April 15, and the managers will submit requested information by July 15. The audit work plan will be completed by September 30, published, and made available to OMB, GAO, DCAA, and other interested parties. Planned audits should be submitted using the Audit Lead Sheet/Planned Audit Profile discussed later in this chapter, and in accordance with the procedures described in Chapter 6 for initiating an audit.

The AIGA, DAIGs and regional managers will perform the priority ranking described in Exhibit B (A:AM05EXB.WPF) using risk assessment procedures discussed in Chapter 21, Exhibit A (A:AM21EXA.WPF). The results are consolidated by region. Audits for each region are incorporated into the work plan taking into consideration availability of resources from the highest ranking audit downward until all available flexible staff days for the fiscal year are accounted for.

e. Changes in Published Work Plan - All work plan changes (additions, cancellations and terminations) must be approved by Headquarters before action is taken. Additions are accomplished through submission of a Planned Audit Profile. Cancellations and terminations generally require a memo. Where cancellations are required, audits with the lowest priorities should be considered first. Termination of an audit may be accomplished by Headquarters approval of the end of survey decision contract, or by memorandum if termination is either before or after the survey is completed.

C. IDENTIFYING AUDIT IDEAS AND NEEDS

The basic thrust of the planning process is to apply OA's available audit resources to obtain maximum audit coverage and avoid unnecessary duplication of audit effort. The specific audits enumerated in the annual work plan come from a variety of sources, all of which play an important role in determining which audits will be performed and the benefit to be achieved.

1. Recurring Audit Requirements. Statutory and regulatory requirements prescribe that certain audits be performed. These requirements may originate from such sources as Congress, OMB, GAO, or the terms of DOE's contracts. In other cases, the audits are not mandatory, but represent areas where the OIG has made a commitment to provide continuing audit coverage. Regional Managers are responsible for ensuring that these requirements have been identified and reflected in the annual audit work plan.

a. Federal Managers' Financial Integrity Act - Much of the audit work done in the financial management area is required by law. The single largest undertaking in this area is the annual review required by the FMFIA. Under this Act, the IG is required to review assurance letters prepared by all Departmental elements and express views as to the status of internal controls or material weaknesses within the Department.

b. Use of Superfund Monies - The OIG is required by law to annually audit and report to Congress on DOE's use of Superfund monies. The audit is designed to determine if obligations, disbursements, and reimbursements are reasonable, allowable, and adequately supported.

c. Contract and Preaward Audits - The OIG has to perform some mandatory preaward and incurred cost audits of contractors to satisfy the terms of DOE contracts and to assist contracting officers in negotiating and awarding contracts, making interim payments, or closing out contracts. Planning for these audits is also addressed in the section of this Chapter on "Requests for Contract Audit Services."

d. Grant Audits - Some audits of state and local governments are required by OMB Circular A-128. The OIG has oversight responsibility for those audits where DOE is designated as the cognizant agency.

e. VANEA Audits - At the end of each fiscal year, integrated contractors are required to submit a Voucher Accounting for Net Expenditures Accrued (VANEA) which includes the contractor's certification that the costs claimed represent allowable contract costs. In accordance with DOE Order 2200.8B, "Accounting Systems, Organizations, and Reporting," issued 3-30-89, the OIG is responsible for periodically examining the reliability of the internal controls used by the contractor and the affected Field Element to assure that only costs allowable under terms of the contract are claimed and reimbursed.

f. Chief Financial Officers Act of 1990 - The Chief Financial Officers Act of 1990 contains provisions for preparation of certain financial statements and the submission of those statements to the Director of OMB. Each designated financial statement must be audited in accordance with generally accepted Government auditing standards by the IG or by an independent external auditor.

g. Other Recurring Audits - A number of other audits must be considered while preparing the annual work plan. These include consultant services, year-end spending, and the Lobbying Act.

2. Self-Initiated Audits. Many of the OA audit proposals are developed by auditors in the field who have noted weaknesses in internal controls; susceptibility to fraud, waste, or abuse; new procedures or changed conditions; and operational results. Other ideas result from more formalized planning surveys.

a. Audit Lead Sheet/Planned Audit Profile - A single document is used for both Audit Lead Sheet and Planned Audit Profile. (See Exhibit A for

format, A:AM05EXA.WPF, and Exhibit B for instructions for preparing the document, A:AM05EXB.WPF.)

(1) Audit Lead Sheet - Auditors are encouraged to submit audit lead sheets to their regional management whenever they spot a potential audit issue. Even partially developed ideas, which may not have all finding elements, should be submitted, as they may be refined later. A lead sheet consists of page 1 of the Audit Lead Sheet/Planned Audit Profile. Audit Lead Sheets may be submitted as part of the annual planning process or at any other time during the year.

(2) Planned Audit Profile - When an Audit Lead Sheet is proposed by a Region to be accomplished, it is upgraded to a Planned Audit Profile. Ideas that reach the stage where they are considered viable potential audits should be formalized in Planned Audit Profiles. This is accomplished by revising the Audit Lead Sheet (page 1) to reflect the most recent, complete information available and completing pages 2 and 3. At this stage, finding elements are laid out, resource requirements are projected, and approvals are obtained.

b. Planning Surveys - In some cases, the AIGA will designate general subject areas for extensive survey work. These surveys are used to obtain information about particular subject areas and to develop strategies for further audit work. Timeframes and reporting objectives for these planning surveys will be determined on a case-by-case basis. In addition, Regional Managers can authorize up to two weeks of survey work in order to develop audit ideas without establishing a separate job code or reporting requirement.

3. Requests for Contract Audit Services. Auditing preaward proposals and contracts in the Department is the primary responsibility of DCAA, and only a small number of such audits are anticipated annually by AIGA. The procedures for initiating these audits are the same procedures used for performance audits. Specifically, profiles will be required for cost audits, and the project numbers assigned by AP³. Additionally, specific cost audits, when known in advance, should be included in the annual work plan.

Only revised and actual "entrance conference held" and "completed with report" dates will be required entries on the schedule screen (although the cursor will stop on the other milestone fields). A start date will also be required on the start screen to activate the project in the system.

4. Cross-Servicing. To conserve staff resources, promote efficiency, and reduce the impact of audits on the operations of DOE and integrated contractor organizations, the AIGA may establish cross-servicing arrangements under which one Federal agency will make or oversee audits for other agencies. Such arrangements will be made when it is in the best interest of DOE and the Federal Government.

a. DOE as Audit Representative - OA will be the DOE audit representative at all DOE installations and at all integrated contractor plants and all other contractor plants whose DOE funded business represents more than 50 percent of the contractor's Government business. An exception to this policy is when a DOE contractor is remotely located from a DOE installation, in which

case the agency that audits the contractor's other government contracts may audit DOE contracts, provided a cross-servicing agreement has been signed between the AIGA and the designated representative of that audit agency.

b. Other Agencies as Audit Representative - OA will establish cross-servicing arrangements with other Federal audit organizations to do all preaward and postaward audits at contractor facilities remotely located from a DOE installation, provided the other Federal agency has an audit staff near the remotely situated contractor facility or, as a customary practice, audits contracts at that location. Otherwise, OA will perform the audit work.

5. Referrals or Requests for Assistance from Investigations and Inspections. Regional Offices occasionally receive referrals or requests for audit assistance from the AIGI or AIG/IA. Procedures for handling such referrals or requests are discussed below.

a. Referrals - Regional Managers may accept referrals from Investigations or Inspections if workload allows and prior approval is granted by the AIGA. Referrals must be in writing with a copy sent to the AIGA. Verbal referrals may not be accepted. Once the AIGA has approved the referral, the Regional Manager should respond to Investigations or Inspections using the format in exhibit C (A:AM05EXC.WPF).

b. Requests for Audit Assistance - Occasionally, Regional Managers may be requested to provide various audit services to Investigations or Inspections. Regional Managers may use their discretion in deciding which requests to honor, but should consider workload, priority, and resource availability.

6. Referrals or Requests for Assistance from Other Agencies. Regional Offices may also receive referrals or requests for assistance from other agencies, particularly from other OIGs. These requests should be handled in the same manner as those received from Investigations or Inspections.

D. PLANNING CONSIDERATIONS FOR SPECIFIC AUDITS

A number of planning factors must be dealt with in developing audit ideas and at the beginning of each audit. Consideration of these factors is expressly required by Yellow Book standards and should be reflected in the Planned Audit Profiles and Audit Programs. Exhibit D (A:AM05EXD.WPF) provides a summary comparison of audit requirements for financial audits versus those for performance audits.

1. Audit Objectives, Scope, and Methodology. The first step in planning an audit is to carefully define the audit objectives. Simply stated, an objective is a precisely worded question that the audit is trying to answer. The statement of audit objectives should clearly articulate what the audit is to accomplish. The audit objectives will affect every phase of the audit, from the selection of scope, methodology, and staff, to the conduct of the audit, and the timing and nature of the report to be issued. Time invested in determining an audit's objectives is usually time well spent because an audit with clear objectives is unlikely to result in wasted resources, delays, and poor quality reports. Clear objectives are also critically important in determining the nature and extent of testing that must be done to satisfy the

requirements for examining internal control and compliance with laws and regulations, as discussed below.

a. Audit objectives are important in deciding on the scope of an audit. Scope includes such factors as the time period to be covered, extent of testing, and locations or activities to be audited.

b. Methodology refers to the process used to gather and analyze data and to reach conclusions and recommendations. The methodology selected needs to provide evidence that will achieve the objectives of the audit. Methodology involves consideration of data sources and techniques of analysis. Specific methodologies will be detailed in the audit program prepared for each audit.

c. The AIC is required to address audit objectives, scope, and methodology in preparing each audit program. As a minimum, audit programs are to be approved by an Audit Director.

2. Criteria for Assessing Performance. Criteria are standards against which the auditee's performance or financial information can be assessed. Types of criteria include laws, regulations, DOE Orders, procedures, hand-books, public statements, and so forth. Criteria is necessary to establish whether a program or office is doing what it is supposed to be doing ("what should be"). The Yellow Book states that criteria should be "reasonable and attainable" based on the situation being audited.

3. Coordination With Other Auditors. OA must coordinate with a number of other audit organizations, including external groups such as GAO and DCAA, as well as internal auditors employed by DOE. In addition, the regional offices must closely coordinate with one another to avoid duplication and inefficiencies.

a. External Audit Groups - A number of other organizations have responsibility to perform audits and reviews within DOE and its contract universe. Chief among these are GAO and DCAA. Before any new work is begun, it is important for auditors to check with these organizations to ensure that they are aware of recently completed, ongoing, or planned work in the same or related areas. This is important to avoid duplication and make optimum use of OA's limited resources. Generally, the Regional Manager should establish lines of communication with these external agencies and be aware of their activities related to DOE. This does not, however, relieve the AIC from the responsibility to know about other organizations' audits and reviews relevant to his or her current assignment.

The AIGA may have occasion to use the work of another independent auditor as part of the basis of audit conclusions we reach. In this situation, the AIC is required to

- o inquire about the professional reputation and standing of the other auditor; and
- o obtain representation from the other auditor regarding independence.

b. Internal Auditors - Most DOE integrated contractors are required by the terms of their contracts to have internal auditors. These auditors are required to plan and perform audits of functional areas based upon a risk assessment, as detailed in Part VI of this Manual. Some other DOE facilities, such as Pittsburgh and Schenectady Naval Reactors, have resident internal auditors (or management review teams) employed by DOE. Each Regional Manager is responsible for coordinating with these internal auditors, for periodically reviewing their work, and for taking such work into account when planning audits.

(1) Relying on the Work of Internal Auditors. With respect to the work of internal auditors (see SAS 65), the AIC is required to

- o obtain an understanding of the internal audit function;
- o evaluate and test the effectiveness of internal auditors' work in determining the nature, timing, and extent of audit procedures;
- o assess the competence and objectivity of the internal auditors and the effect of the internal auditors' work on the AIGA audit (this can be accomplished by examining and testing the internal auditor's work);
- o supervise, review, evaluate, and test the work performed by internal auditors when the internal auditors are providing direct assistance to the AIGA audit; and
- o assure that all judgments are those of the AIGA, not the internal auditor.

(2) Transaction Testing at M&O Contractors. When planning audit steps at an M&O contractor site, the AIC should consider transaction testing done in other--usually internal--audits that are part of the acceptable risk ranking methodology. To the extent that these tests are relevant to the current audit objective and are still considered timely, the AIC may choose to rely upon the results of such tests.

c. Coordination Within OA - The nature of OA's work is such that the Regional Managers have a great deal of latitude and responsibility with respect to planning and executing audit work. Essentially, each Regional Manager is responsible for assuring adequate and efficient audit coverage for the DOE activities within his or her geographic area. However, audit work in one region frequently requires information from or travel to another region. When this occurs, auditors are responsible for contacting and coordinating with the other region.

(1) An AIC or other auditor should first contact his or her Audit Director or ARM to discuss the coordination needed with another region, then make any additional contacts in the other region deemed necessary. Normally, coordination between regions should occur at the Audit Director level or higher to ensure that the individuals involved are familiar with most prior or ongoing audit work.

(2) Audit Directors and ARMs are responsible for ensuring that their Regional Managers are kept fully apprised of all audit activity affecting their region and to assure that audit objectives are accomplished with the maximum possible efficiency.

(3) Multi-location audits entail a specialized approach to coordination discussed in chapter 6, section E.

d. Audit Follow-up - An important element of coordination is audit follow-up. In the early planning stages of any OA audit, the AIC is required to identify any recently completed reviews or audits covering the same or related subject matter. Such reviews may have been conducted by OA, other DOE internal audit groups, or external audit groups. The audit program should include steps to assure that recommendations from such previous reports have been addressed.

4. Identifying Unallowable Costs. Every audit of an M&O contractor must include audit steps to identify unallowable costs.

5. Coordination With Investigations. Early in the audit, the AIC or other regional representative should contact Investigations and discuss the audit. This must be accomplished sufficiently early so that any information obtained can be used to help develop audit findings or alter verification work steps. Early coordination will also help to avoid duplication of effort. Contact with Investigations must be documented in the workpapers.

6. Staffing Considerations. Staffing involves the training and expertise of those who will carry out an assignment as well as the number of people needed by grade and location. Staff capabilities affect the objectives, scope, methodology, cost and timing of audits. Also, because of resource limitations, some audits may have to be staffed with contractor audit personnel or other external staff.

a. Assigning Staff to Audits - Regional Managers are responsible for assuring that assigned staff have the appropriate skills and knowledge for the job. Consideration should be given to the technical nature of the assignment, the relevant abilities of the auditor, and on-the-job training (OJT) requirements.

b. External Staffing Considerations - Where specialized training or skills are called for that are unavailable on the audit staff, experts or consultants may be used. In addition, some audits may need to be staffed with contractor audit personnel or other external staff because of OA resource limitations.

c. Yellow Book Guidelines on Staffing - The Yellow Book has established specific staff qualification requirements for financial statement audits that lead to an expression of an opinion. However, financial related and performance audits also need to be staffed with auditors who have the requisite qualifications and training. The chart below illustrates options for staffing most OA audits.

TYPE OF AUDIT	CPA FIRM	OTHER CONTRACTOR/ CONSULTANT	OA AUDITORS
Financial Statement	X		X
Financial Related	X	X	X
Performance	X	X	X

7. Compliance With Laws and Regulations. The 1938 Yellow Book revisions recognize an increasing expectation that the audit community should strengthen its efforts to evaluate compliance with laws and regulations and detect and report significant illegal acts and abuses. All audits are to be properly planned and include steps to provide reasonable assurance--not absolute or complete--that material instances of noncompliance that directly relate to the assignment's objectives are detected and reported.

a. Yellow Book Standards - For both performance and financial audits, the Yellow Book requires auditors to

- o determine if assignment objectives require that tests of compliance with laws and regulations be performed;
- o identify laws and regulations that apply to the entity being audited and that are relevant to assignment objectives;
- o assess the risk that noncompliance with these laws and regulations could significantly affect the program operations or financial statements being audited;
- o consider whether internal controls deter or help detect noncompliance;
- o design work steps to reasonably assure the (1) entity's compliance with relevant laws and regulations and (2) detection of errors, irregularities, abuse, or illegal acts that could significantly affect the assignment objectives;
- o exercise appropriate caution in reviewing illegal acts so as not to interfere with potential future investigations and/or legal proceedings (see chapter 4);
- o promptly prepare an audit report that includes all significant or material instances of noncompliance (see chapter 10); and
- o promptly report all illegal acts that could result in criminal prosecution (see chapter 10).

The Yellow Book also requires that financial audits be performed in accordance with the fieldwork and reporting standards prescribed by the AICPA. The AICPA has issued a series of SASs, and the following standards are particularly applicable to detecting and reporting noncompliance with laws and regulations on financial audits:

- o "Compliance Auditing Applicable to Government Entities and Other Recipients of Governmental Financial Assistance" (SAS 68),
- o "Consideration of the Internal Control Structure in a Financial Statement Audit" (SAS 55),
- o "Illegal Acts by Clients" (SAS 54), and
- o "The Auditor's Responsibilities to Detect and Report Errors and Irregularities" (SAS 53).

b. Importance of Assignment Objectives - The audit objectives are key in determining the scope of compliance testing to be performed. Objectives should be defined as precisely as possible to preclude unnecessary work, while still meeting the purpose of the audit. Audit objectives should be clearly stated and fully understood. Only those tests of compliance necessary to satisfy the audit objectives should be performed.

Where assessment of compliance is called for by the audit objectives, the audit program must include steps and procedures that will provide reasonable assurance that the audited entity has adhered to the requirements of laws and regulations which, if not followed, could significantly affect the audit results. The audit must also be designed to provide reasonable assurance of detecting abuse or illegal acts that could significantly affect the audit objectives. This standard relies heavily on the auditor's professional judgment in determining whether and the extent to which compliance testing is necessary. The AIC is responsible for incorporating the necessary steps into the approved audit program.

c. Identifying Applicable Laws and Regulations - During the early phase of an audit where compliance assessment is called for by the audit objectives, auditors should identify the laws and regulations that apply to the subject area and might significantly affect the objectives.

At a minimum, auditors must discuss relevant laws and regulations with officials of the audited entity and document this discussion in the workpapers. The workpapers should also contain a listing of the laws, regulations, and other requirements determined to be pertinent to the audit objectives. Auditors are required to consult with General Counsel (through the OIG's legal counsel) when questions arise concerning application and the interpretation of laws and regulations.

The auditor's consideration should include general laws and regulations governing the subject matter, as well as more specific implementing requirements, such as DOE Orders. An audit of procurement activities, for example, might include consideration of the Federal Acquisition Regulations or the Competition-in-Contracting Act, as well as the DOE Acquisition Regulations.

Auditors are also required to identify, and document in the workpapers, laws and regulations which, if violated, may have an indirect and material affect on the audit objectives. Examples of such laws and regulations could include environmental requirements, fair labor standards, and equal employment opportunity.

d. Assessing Risk - The Yellow Book requires that auditors assess, for each legal or regulatory requirement relevant to the audit objectives, the risk that abuse and illegal acts could occur. The risk assessment determines the probability that material noncompliance or abuse could occur and not be prevented or detected in a timely manner by internal controls. The assessment evaluates (1) the inherent risk of a law or regulation to noncompliance and abuse before considering internal controls and (2) whether internal controls will prevent or detect noncompliance and abuse.

(1) Types of Risk. The table below is helpful in understanding the relationship among the different types of risk and the extent of compliance testing required. The types of risk are defined as follows:

- o Inherent risk is the probability that a law or regulation related to assignment objectives will not be complied with or that the area being reviewed is highly susceptible to noncompliance.
- o Control risk is the risk that internal control structure will not detect or prevent non-compliance.
- o Detection risk is the risk that the auditor's procedures will lead to an erroneous conclusion about compliance with laws and regulations.

RISK/TESTING RELATIONSHIPS

ASSESS INHERENT RISK	EVALUATE INTERNAL CONTROLS	ASSESS CONTROL RISK	ASSESS VULNERABILITY AND DETERMINE TESTING EXTENT	ASSESS DETECTION RISK
HIGH	WEAK/HIGH		HIGH	LOW
	ADEQUATE/MODERATE		MODERATE TO HIGH	MODERATE
	STRONG/LOW		LOW TO MODERATE	HIGH
MODERATE	WEAK/HIGH		MODERATE TO HIGH	LOW
	ADEQUATE/MODERATE		MODERATE	MODERATE
	STRONG/LOW		LOW	HIGH
LOW	WEAK/HIGH		LOW TO MODERATE	LOW
	ADEQUATE/MODERATE		LOW	MODERATE
	STRONG/LOW		VERY LOW	HIGH

As the above table indicates, higher inherent risk and weaker internal controls require increased compliance testing. Auditors should also be aware that reduced testing, while highly desirable given scarce audit resources, by definition increases detection risk.

(2) Characteristics of Illegal Acts. In order to accurately gauge the inherent risk that noncompliance with laws or regulations relevant to audit objectives may occur without being prevented or detected, the auditor must be alert for "characteristics" of illegal acts. The professional literature speaks of characteristics, but also uses the terms "instances" and "indicators" of illegal acts. For OA purposes, the term characteristic will be used as a collective term to define a potential illegal act. A characteristic is an observed control weakness, personal behavior, relationship, or deviation in recordkeeping that raises skepticism about the fidelity of a function in which there is an opportunity for illegal acts to occur. (See also exhibit D, A:AM05EXD.WPF.)

Characteristics can be opportunities, such as

- o activities dominated and controlled by a single person or small group;
- o complex transactions; or
- o a mix of contracts.

Characteristics can also be indicators, such as

- o altered, missing, or otherwise suspect accounting records;
- o unreasonable explanations to inquiries by auditors;
- o auditee annoyance at reasonable questions by auditors;
- o extravagant lifestyle of employees; or
- o auditee tactics to delay the audit.

For each audit where compliance assessment is necessary, the AIC is responsible for documenting in the workpapers any characteristics (opportunities or indicators) of illegal acts noted. If any characteristics are observed, audit steps must be designed (a) to determine whether the acts occurred and (b) if so, to determine the extent to which these acts significantly affect the audit results. These steps should be documented in the approved audit program or the workpapers.

e. Internal Controls Testing - Internal controls must be assessed when necessary to satisfy the objectives of a performance audit. (Internal control assessment as related to financial audits is discussed in section 8 below.) Once the auditor identifies inherent risks, an assessment must be made as to the effectiveness of internal controls designed to prevent or detect non-compliance. Internal controls consist of policies and procedures used to provide reasonable assurance that goals and objectives are met; resources are adequately safeguarded, efficiently utilized, and reliably accounted for; and laws and regulations are complied with.

Where internal control assessment is called for by the audit objectives, the AIC is required to

- o identify and document internal control policies that management has designed to ensure that the relevant laws and regulations are complied with,
- o observe the control environment and document unusual observations in the workpapers,
- o identify key internal control procedures that management has established to achieve objectives,
- o test control procedures, and
- o identify needed follow-on actions.

To re-emphasize, clearly defined audit objectives are critical in determining (1) if an assessment of compliance and internal controls is necessary, and (2) if so, the extent of assessment and audit steps required. For every performance audit, the AIC is required to document in the workpapers the determination as to whether compliance and internal control assessments are required in light of the audit objectives and the results of any required assessment.

8. Assessing Internal Controls--Financial Audits. With respect to financial audits, the Yellow Book explicitly incorporates the provisions of SAS 55. For financial audits, auditors are required to become familiar with SAS 55 and document compliance with that standard in the workpapers. The auditor should note that while the provisions of SAS 55 are required in financial audits, they are also a good blueprint for a successful assessment of internal controls when called for by the objectives of a performance audit. In accordance with the major requirements of SAS 55, for financial audits, the AIC must

- o understand the internal control structure and determine whether related policies and procedures are in operation;
- o document the understanding of the internal control structure;
- o assess control risk related to the internal control structure;
- o document the basis for the assessed maximum level of control risk;
- o consider performing tests of controls;
- o assess control risk related to tests of controls;
- o document the basis for any assessed level of control risk at less than maximum level; and
- o design substantive tests based on assessed level of control risk.

a. Elements of Internal Control Structure - SAS 55 breaks down internal control structure into the elements of (1) control environment, (2) accounting system, and (3) control procedures.

(1) Control Environment. The control environment can be thought of as the overall attitude of management concerning the importance of control. This includes management's philosophy and operating style, the organizational structure of the audited entity, and management's control methods.

(2) Accounting System. An entity's accounting system includes the methods and records established to identify, assemble, analyze, classify, record, and report transactions and to maintain accountability.

(3) Control Procedures. Control procedures are those policies and procedures--in addition to the control environment and accounting system--established to provide reasonable assurance that specific objectives will be achieved. Examples of control procedures would include

- o proper authorization of transactions;
- o design, use, and control of accounting documents;
- o safeguard of assets;

- o segregation of duties; and
- o independent checks.

b. Documenting Understanding of the Internal Control Structure

Auditors are required to document in the workpapers their understanding of the internal control structure. Methods of documentation include the preparation of flowcharts, internal control questionnaires, and narrative descriptions. Auditors must use professional judgment to determine which method(s) should be used to document the understanding.

c. Assessing and Documenting Control Risk - Auditors must understand all elements of risk (see table on page 5-12), including inherent risk, control risk, and detection risk. This understanding, including an assessment of relevant internal controls and the likelihood that such controls will not be effective, must be documented in the workpapers. If maximum risk is assessed with little potential for a reduced level of assessment, the auditor should forgo testing of controls and proceed to substantive testing. Specific guidance for the assessment and documentation of control risk can be found in SAS 55.

d. Tests of Controls and Reassessment of Risk - If, after assessing control risk, the AIC determines that the internal control structure cannot be relied on, no tests of controls are required and auditors may proceed to substantive testing of accounts and balances. However, if the AIC believes that the internal control structure can be relied on, tests of controls are required. Testing consists of (1) evaluating the design effectiveness of the controls (are the controls in place?), and (2) testing the operational effectiveness of the controls (are they working as intended?). Auditors must document these tests in the workpapers.

Based on the results of the tests of controls, the AIC must determine whether the initial assessment of control risk was accurate, and whether the controls are still considered reliable. This reassessment will determine the extent of substantive testing required to complete the audit. Auditors must carefully document the reassessment, based on evidence gathered from the tests of controls.

e. Designing Substantive Tests - Based on the assessment of (1) inherent risk, and (2) control risk, the auditor must then determine an acceptable level of detection risk and design substantive tests accordingly. Substantive tests are defined as tests of details and analytical procedures performed to detect material misstatements in the account balance, transaction class, and disclosure components of financial statements.

9. Materiality and Significance. The Yellow Book requires the consideration of materiality and significance in planning the audit and selecting the methodology. Materiality is also important in determining whether a matter requires disclosure in a report.

Because those who deal with public funds assume a distinct stewardship responsibility, the materiality level or threshold of acceptable risk may be lower than in similar audits in the private sector. In planning the audit, the AIC may consider the following.

- o Amount of revenues and expenditures.
- o Newness of the activity or changes in its conditions.
- o Adequacy of internal controls.
- o Results of prior audits.
- o Level and extent of review or other form of independent oversight.
- o Adequacy of the internal controls for ensuring compliance with laws and regulations.
- o Management's adherence to applicable laws and regulations.
- o Audit report user's expectations.
- o Public perceptions and political sensitivity of the areas under audit.
- o Audit requirements.

The 1988 revision of the Yellow Book adds a great deal of emphasis to the areas of compliance with applicable laws and regulations and internal controls. In planning the audit, auditors must still consider materiality and significance. However, once discovered, the materiality threshold for reporting fraud, illegalities, and abuse is zero-- i.e., if found, it must be reported.

PROJECT NO: _____

AUDIT LEAD SHEET/PLANNED AUDIT PROFILE

File Name _____ Preparer _____

1.	<table border="1"><tr><td>☐</td><td>AUDIT LEAD SHEET</td></tr><tr><td>☐</td><td>PLANNED AUDIT PROFILE</td></tr></table>	☐	AUDIT LEAD SHEET	☐	PLANNED AUDIT PROFILE	ORIGINAL	_____	REVISED	_____	DATE: ____/____/____
☐	AUDIT LEAD SHEET									
☐	PLANNED AUDIT PROFILE									
2. AUDIT TITLE: _____

3. SHORT TITLE: _____
4. RESPONSIBLE OFFICE & CODE: _____
5. REASONS FOR SELECTION AND BACKGROUND:
6. AUDIT OBJECTIVES:
7. AUDIT APPROACH: (Scope and methodology)
8. POTENTIAL FINDING(S): (Asserted criteria, condition, cause, and effect.)

NOTE: ITEMS ON NEXT PAGE NOT REQUIRED FOR AN AUDIT LEAD SHEET; HOWEVER, COMPLETE FOR A PLANNED AUDIT PROFILE.

9. PRIORITY RANKING: _____10. JUSTIFICATION FOR PRIORITY: _____

11. PLANNED DATES: ENTRANCE CONFERENCE: ____/____/____
SURVEY COMPLETION: ____/____/____
REPORT ISSUANCE: ____/____/____

Elapsed Days: _____

12. STAFF DAYS REQUIRED:

Staff Days:	FY__	FY__	FY__	TOTAL
IG Days	_____	_____	_____	_____
IPA Days	_____	_____	_____	_____
Total	_____	_____	_____	_____

13. CLASSIFICATION OF AUDIT: Financial _____ Performance _____14. TYPE OF AUDIT: _____15. PROGRAM CODE: _____16. MAJOR ISSUE AREA: _____17. DOE ORGANIZATION: _____18. AUDIT LOCATIONS: () Single Site () Multi-Site () Multi-Region

Location(s) to be audited: _____

19. APPROVALS:

Preparer: _____ Date _____

Reviewer: _____ Date _____

Regional Manager: _____ Date _____

DAIG/AP3: _____ Date _____

DAIG/AO: _____ Date _____

AIGA: _____ Date _____

Instructions for Preparing the
Audit Lead Sheet/Planned Audit Profile

1. Original/Revised/Date. Indicate whether this document is an audit lead sheet or a planned audit profile, an original, or a revision or a previously submitted lead or profile, and give the current date. Ap³ will assign the project number.
2. Audit Title. Enter the complete audit title.
3. Short Title. Enter an abbreviated audit title (limited to 35 characters & spaces.)
4. Responsible Office & Code. Office codes are as follows:

ALA ALBUQUERQUE AUDIT GROUP	EMA EASTERN REGION MANAGER	PLA PORTLAND AUDIT GROUP
AMA DAIG/AO	FRA FERC AUDIT GROUP	PRA PRINCETON AUDIT GROUP
ATA ADP & TECHNICAL SUPPORT	IFA IDAHO FALLS AUDIT GROUP	PTA PITTSBURGH AUDIT GROUP
CFA WASHINGTON AUDIT GROUP	IGA ASSISTANT IG FOR AUDITS	RLA RICHLAND AUDIT GROUP
CGA GERMANTOWN AUDIT GROUP	LAA LOS ALAMOS AUDIT GROUP	SRA SAVANNAH RIV. AUDIT
CHA CHICAGO AUDIT GROUP	LLA L. LIVERMORE AUDIT GROUP	WMA WESTERN REGION MANAGER
CMA CAPITAL REGION MANAGER	LVA LAS VEGAS AUDIT GROUP	
CNA CINCINNATI AUDIT GROUP	NOA NEW ORLEANS AUDIT GROUP	
DLA DALLAS AUDIT GROUP	ORA OAK RIDGE AUDIT GROUP	
DNA DENVER AUDIT GROUP	PDA DAIG/AP ³	

5. Reasons for Selection and Background. Briefly describe the condition or situation that requires audit. Explain why this audit is being proposed. This discussion may include reference to previous audit work in the same area.
6. Audit Objectives. Enter a precisely worded question that the audit is to answer. The audit objectives should clearly articulate what the audit is to accomplish. The auditor should bear in mind that the objectives will have a significant impact on the amount of testing for compliance with laws and regulations, and internal controls, that is required.
7. Audit Approach. This section should discuss the scope of coverage and include a brief description of the methodology for achieving the audit objectives.
8. Potential Findings. The preparer should lay out potential findings in as much detail as possible. All elements, particularly cause and effect, may not be apparent at this stage.

NOTE: AUDIT LEAD SHEETS ONLY NEED TO BE COMPLETED THROUGH ITEM 8. TO PREPARE A PLANNED AUDIT PROFILE, REVISE PAGE 1 TO REFLECT THE MOST RECENT COMPLETE INFORMATION AVAILABLE AND COMPLETE REMAINDER OF FORM.

9. Priority Ranking. Each proposed audit will be assigned a priority based on ranking factors. The following factors will be determined for each proposed audit:

<u>Factor</u>	<u>Criteria for Factor</u>
---------------	----------------------------

A	» OMB High Risk Area or
» IG Interest or
» Secretarial Interest
B	» Sizeable Program or
» Significant Monetary Impact
C	» Vulnerability to Fraud and Abuse
D	» Relationship to known audit trends (based on prior audits)

After appropriate factors are determined for each proposed audit, the following priorities will be assigned:

<u>Priority</u>	<u>Explanation</u>
-----------------	--------------------

1.	» Must incorporate Factors A <u>and</u> B, plus additional factor(s) if applicable.
2.	» Incorporates Factor A <u>or</u> Factor B, plus one or more additional factors.
3.	» Incorporates one or more factors.
10. Justification. Provide a narrative justification for the priority ranking in item 9 or any explanation of priority factors, especially if N/A has been indicated, that will support the need for or urgency of the proposed audit.
11. Dates. Refer to chapter 6 of the Audit Manual for maximum allowed elapsed days.
12. Estimated Time Required. Enter the expected number of required days by fiscal year for both IG and IPA/CPA staff.
13. Classification of Audit. Place an "x" after either financial or performance.

14. Type of Audit. Enter the appropriate code from the following list:

CODE	TYPE OF AUDIT	CODE	TYPE OF AUDIT	CODE	TYPE OF AUDIT
CAL	CNTR-ADV PAYMENT/LOC	CPP	CNTR-PROGRESS PAYMENT	GIC	GRNT-INCURRED COSTS
CCA	CNTR-ACCTG. SYSTEMS	CRT	CNTR- TERMINATION	GOO	GRNT-OTHER
CDP	CNTR-DEFECTIVE PRICE	EAE	ECONOMY & EFFICIENCY	GPA	GRNT-PREAWARD
CFC	CNTR-FINAN. CAPACITY	FAC	FINANCE & COMPLIANCE	GPP	GRNT-PROGRESS PAYMENT
CFO	CFO ACT AUDITS	FIA	FMFIA	GRT	GRNT-TERMINATION
CFP	CNTR-FORWARD PRICE	FSA	FIN STATEMENT AUDITS	OTH	OTHER
CIC	CNTR-INCURRED COSTS	GAL	GRNT-ADV PAYMENTS	PRR	PROGRAM RESULTS
COO	CNTR-OTHER	GCA	GRNT-ACCTG. SYSTEMS	VAN	VANEAS
CPA	CNTR-PREAWARD	GFC	GRNT-FIN. CAPABILITY	YEA	YEAR-END STATEMENTS

15. Program Code: Enter the program code from the following

AFP	ALTERNATIVE FUELS PRODUCTION	ECN	ENERGY CONSERVATION	RES	ENERGY SUPPLY R&D
APA	ALASKA POWER ADMINISTRATION	EIN	ENERGY INFORMATION	RGT	GEO THERMAL ENERGY
ASA	ASSIST AUDITS	EPE	EMERGENCY PREPAREDNESS & ENERGY REGULATION	RHP	HYDROPOWER
BPA	BONNEVILLE POWER ADMINISTRATION	EPR	ENERGY PRODUCTION	RMF	FUSION ENERGY
CRB	COLORADO RIVER BASIN MKT FUND, WAPA	FRC	FEDERAL ENERGY REG COM	RNF	NUCLEAR ENERGY
DEF	ATOMIC ENERGY DEFENSE	FRD	FOSSIL ENERGY R&D	ROE	OTHER ENERGY SUPPLY R&D
DIC	INERTIAL CONFINEMENT FUSION	GRD	GEO THERMAL RES DEV FUND	RSE	SOLAR ENERGY
DMP	MATERIALS PRODUCTION	GSR	GENERAL SCIENCE & RES	RSH	ENVIRON, SAFETY & HEALTH
DNR	NAVAL REACTOR DEVELOPMENT	MPA	MULTI-PROGRAM ACTIVITIES	RSS	ENERGY STORAGE SYSTEMS
DNS	NUCLEAR SAFEGUARDS AND SECURITY	NWD	NUCLEAR WASTE DISPOSAL	RST	SPILL TEST FACILITY
DPA	DEPARTMENTAL ADMINISTRATION	OTH	OTHER	SEP	SOUTHEASTERN POWER ADMIN
DRP	REIMBURSABLE PROGRAMS	PTS	PMTS TO STATES--FED POW	SPR	STRATEGIC PETROLEUM RES
DSI	SECURITY INVESTIGATIONS	RBE	BIOLOGICAL ENVIRON RES	SWP	SOUTHWESTERN POWER ADMIN
DVC	VERIFICATION AND CONTROL TECH	REE	ELEC ENERGY SYSTEMS	TFA	TRUST FUND--ADVANCES FOR COOPERATIVE WORK
DWA	WEAPONS ACTIVITIES			USE	URANIUM SUPPLY & ENRICH
DWB	WASTE MANAGEMENT			WAP	WESTERN AREA POWER ADMIN

16. Major Issue Area. Enter the code for the major issue area from the following list:

001	ENVIRONMENT, SAFETY AND HEALTH	007	SUPERCONDUCTING SUPER COLL	012	ADMIN. SAFEGUARDS
002	WEAPONS PROGRAMS	008	POWER MARKETING ADMIN	080	WORK FOR OTHER FED AGC
003	NUCLEAR WASTE DISPOSAL	009	PROCUREMENT & GRANTS MGT		
005	SAFEGUARDS AND SECURITY	010	EXPANSION OF LAB MISSIONS		
006	STRATEGIC PETROLEUM RESERVE	011	FINANCIAL MANAGEMENT		

17. DOE Organization. Enter the DOE Organization Code from the following list.

CODE	LOCATION DESCRIPTION
AAO	AMARILLO AREA OFFICE, AMARILLO, TEXAS
AGO	ARGONNE AREA OFFICE, ARGONNE, ILLINOIS
ALO	ALBUQUERQUE OPERATIONS OFFICE, ALBUQUERQUE, NEW MEXICO
AML	AMES LABORATORY, IOWA STATE UNIVERSITY, AMES, IOWA
ANL	ARGONNE NATIONAL LABORATORY, ARGONNE, ILLINOIS
APA	ALASKA POWER ADMINISTRATION, JUNEAU, ALASKA
ASO	ATLANTA SUPPORT OFFICE, ATLANTA, GEORGIA
ATS	AIR TRANSPORTATION SERVICES, ROSS AVIATION, ALBUQUERQUE, NM
BAD	BILLINGS AREA OFFICE-MURON, SOUTH DAKOTA
BAH	BILLINGS AREA OFFICE, BILLINGS, MONTANA
BAO	BATAVIA AREA OFFICE, BATAVIA, ILLINOIS
BAP	BETTIS ATOMIC POWER LABORATORY, WEST MIFFLIN, PA
BCN	BOULDER CITY AREA OFFICE, BOULDER CITY, NEVADA
BDO	BISMARCK DISTRICT OFFICE, BISMARCK, NORTH DAKOTA
BER	BIOMEDICAL & ENVIRONMENTAL RESEARCH, ALBUQUERQUE, NEW MEXICO
BES	BIOMEDICAL & ENVIRONMENTAL SCIENCE LAB, (UC), LOS ANGELES, CA
BLA	BATES LINEAR ACCELERATOR, MIDDLETOWN, MASSACHUSETTS
BNL	BROOKHAVEN NATIONAL LABORATORY, UPTON, NY
BNY	BROOKHAVEN AREA OFFICE, UPTON, NY
BPA	BONNEVILLE POWER ADMINISTRATION, PORTLAND, OREGON
BPL	BONNEVILLE POWER ADMINISTRATION, LIAISON OFFICE, WASH., DC
BPO	BARTLESVILLE PROJECT OFFICE, BARTLESVILLE, OKLAHOMA
BPR	BUTTE PROJECT OFFICE, NEW PRODUCTION REACTORS, IDAHO FALLS
BSH	BOSTON SUPPORT OFFICE, BOSTON, MASSACHUSETTS
CEB	CONTINUOUS ELECTRON BEAM ACCELERATOR FACILITY, NEWPORT NEWS
CFE	CENTER FOR ENERGY
CFF	CFFF (U OF TENN)
CHO	CHICAGO OPERATIONS OFFICE, CHICAGO, ILLINOIS
CSO	CHICAGO SUPPORT OFFICE, CHICAGO, ILLINOIS
DAO	DAYTON AREA OFFICE, MIAMISBURG, OHIO
DOT	DALLAS SUPPORT OFFICE, DALLAS, TEXAS
DSC	DENVER SUPPORT OFFICE, DENVER, COLORADO
EBR	EXPERIMENTAL BREEDER REACTOR II, ARGONNE-WEST, IDAHO FALLS
ENL	ENVIRONMENTAL MEASUREMENTS LABORATORY, NEW YORK, NY
EMO	EASTERN MEASUREMENTS OFFICE, EG&G, ANDREWS AFB, MARYLAND
EPO	EKLUTNA PROJECT OFFICE, PALMER, ALASKA
ERD	ECONOMIC REGULATORY ADMINISTRATION, DALLAS, TEXAS
ERH	ECONOMIC REGULATORY ADMINISTRATION, HOUSTON, TEXAS
ERL	ENERGY RELATED HEALTH RESEARCH LAB (UC) DAVIS, CA
ETE	ENERGY TECHNOLOGY ENGINEERING CENTER, CANOGA PARK, CA
EXP	EXTRUSION PLANT (RMI)
FER	FEDERAL ENERGY REGULATORY COMMISSION, WASHINGTON, DC
FMP	FERNALD ENVIRONMENTAL MANAGEMENT PROJECT, FERNALD, OHIO
FNL	FERMI NATIONAL ACCELERATOR LABORATORY, BATAVIA, ILLINOIS
FPD	FORT PECK DISTRICT, FORT PECK, MONTANA
FSO	FERNALD ENVIRONMENTAL MANAGEMENT OFFICE, FERNALD, OHIO
GJC	GRAND JUNCTION PROJECT OFFICE, GRAND JUNCTION, COLORADO
GOL	GOLETA OPERATIONS
GYA	GOODYEAR ATOMIC
HAH	HEADQUARTERS, ADMINISTRATION AND HUMAN RESOURCE MANAGEMENT

CODE	LOCATION DESCRIPTION
HBC	HEADQUARTERS, BOARD OF CONTRACT APPEALS
HCE	HEADQUARTERS, CIVILIAN RADIOACTIVE WASTE MANAGEMENT
HCI	HEADQUARTERS, CONGRESSIONAL AND INTERGOVERNMENTAL AFFAIRS
HCR	HEADQUARTERS, CONSERVATION AND RENEWABLE ENERGY
HON	HEADQUARTERS, DEFENSE NUCLEAR SAFETY BOARD
HDP	HEADQUARTERS, DEFENSE PROGRAMS
HDS	HEADQUARTERS, DEPUTY SECRETARY
HDB	HEADQUARTERS, DEPARTMENT ADVISORY COMMITTEES
HEH	HANFORD ENVIRONMENTAL HEALTH FOUNDATION, RICHLAND, WA
HEI	HEADQUARTERS, ENERGY INFORMATION ADMINISTRATION
HEP	HEADQUARTERS, OFFICE OF EMPLOYEE PROTECTION
HER	HEADQUARTERS, ENERGY RESEARCH
HES	HEADQUARTERS, ENVIRONMENT, SAFETY AND HEALTH
HEW	HEADQUARTERS, ENVIRONMENTAL RESTORATION & WASTE MANAGEMENT
HFE	HEADQUARTERS, FOSSIL ENERGY
HFI	HEADQUARTERS, FEDERAL INSPECTOR FOR ALASKA NATURAL GAS TRANS
HFM	HEADQUARTERS, FINANCIAL MANAGEMENT AND CONTROLLER
HGC	HEADQUARTERS, GENERAL COUNSEL
HHA	HEADQUARTERS, HEARINGS AND APPEALS
HIA	HEADQUARTERS, INTERNATIONAL AFFAIRS AND ENERGY EMERGENCIES
HIG	HEADQUARTERS, INSPECTOR GENERAL
HII	HEADQUARTERS, INTELLIGENCE
HMI	HEADQUARTERS, MINORITY ECONOMIC IMPACT
HNE	HEADQUARTERS, NUCLEAR ENERGY
HNP	HEADQUARTERS, NEW PRODUCTION REACTORS
HNS	HEADQUARTERS, NUCLEAR SAFETY
HNW	HEADQUARTERS, NUCLEAR WEAPONS COUNCIL
HPA	HEADQUARTERS, PUBLIC AFFAIRS
HPM	HEADQUARTERS, PROCUREMENT, ASSISTANCE AND PROGRAM MANAGEMENT
HPP	HEADQUARTERS, POLICY, PLANNING AND ANALYSIS
HQR	HEADQUARTERS, THE SECRETARY
HRA	HEADQUARTERS, ECONOMIC REGULATORY ADMINISTRATION
HSA	HEADQUARTERS, SECURITY AFFAIRS
HSD	HEADQUARTERS, SMALL AND DISADVANTAGED BUSINESS UTILIZATION
HSF	HANFORD SITE FACILITY - RICHLAND, WA
HSL	HEADQUARTERS, SCHEDULING AND LOGISTICS
HSP	HEADQUARTERS, SPECIAL PROJECTS
HST	HEADQUARTERS, OFFICE OF SCIENCES AND TECHNOLOGY
HUS	HEADQUARTERS, UNDER SECRETARY
HWA	HEADQUARTERS, WESTERN AREA POWER ADMINISTRATION
HWD	HQS, LIAISON FOR ALASKA, SE, & SW POWER ADMINISTRATIONS
ICP	IDAHO CHEMICAL PROCESSING PLANT, IDAHO FALLS, IDAHO
IDO	IDAHO OPERATIONS OFFICE, IDAHO FALLS, IDAHO
INE	IDAHO NATIONAL ENGINEERING LABORATORY, IDAHO FALLS, IDAHO
INH	INHALATION TOXOLOGY RESEARCH INSTITUTE, LOVELACE, CO
ITR	INHALATION TOXICOLOGY RESEARCH CENTER, ALBUQUERQUE, NM
JIS	JOHNSON ISLAND SUPPORT OFFICE, HONOLULU, HAWAII
KAL	KNOLLS ATOMIC POWER LABORATORY, SCHENECTADY, NY
KAP	KNOLLS ATOMIC POWER LAB., KESSELRING SITE, SCHENECTADY, NY
KAW	KNOLLS ATOMIC POWER LAB, WINDSOR SITE, WINDSOR, CT
KCA	KANSAS CITY AREA OFFICE, KANSAS CITY, MISSOURI
KCP	KANSAS CITY PLANT, KANSAS CITY, MISSOURI

CODE	LOCATION DESCRIPTION
KCS	KANSAS CITY SUPPORT OFFICE, KANSAS CITY, MISSOURI
KIO	KIRTLAND AREA OFFICE, ALBUQUERQUE, NM
KOR	K-25 PLANT, OAK RIDGE, TENNESSEE
LAC	LOVELAND AREA OFFICE, LOVELAND, COLORADO
LAN	LOS ALAMOS NATIONAL LAB., (UC) LOS ALAMOS, NEW MEXICO
LAO	LOS ALAMOS AREA OFFICE, LOS ALAMOS, NEW MEXICO
LBL	LAWRENCE BERKELEY LABORATORY, (UC) BERKELEY, CALIFORNIA
LCO	LOWER COLUMBIA, PORTLAND, OREGON
LLN	LAWRENCE LIVERMORE NATIONAL LAB., (UC) BERKELEY, CALIFORNIA
LOS	LOS ALAMOS OPERATIONS, LOS ALAMOS, NEW MEXICO
LPC	LASER PROJECT OFFICE, LIVERMORE, CALIFORNIA
LPO	LARAMIE PROJECTS OFFICE (NETC), LARAMIE, WYOMING
MDO	MONTROSE DISTRICT OFFICE, MONTROSE, COLORADO
MET	MORGANTOWN ENERGY TECHNOLOGY CENTER, MORGANTOWN, WV
MFM	MOUND FACILITY, MONSANTO
MMD	MAGNETOHYDRODYNAMICS PROJECT OFFICE, BUTTE, MONTANA
MMS	MASON AND HANGER - SILAS
MLO	MOUND LABORATORY, MIAMISBURG, OHIO
MNO	METAIRIE SITE OFFICE, NEW ORLEANS, LA
NAP	NO SITE APPLICABLE
NBL	NEW BRUNSWICK LABORATORY, ARGONNE, ILLINOIS
NDR	NOTRE DAME RADIATION LABORATORY
NNC	NEVADA TEST SITE, LOS ALAMOS NATL LAB (US) MERCURY, NV
NOA	NATIONAL OCEANIC & ATMOSPHERIC ADMINISTRATION, IDAHO FALLS
NPC	NAVAL PETROLEUM RESERVES, CASPER, WYOMING
NPO	NAVAL PETROLEUM & OIL SHALE RESERVES IN CO, UT & WY
NPR	NAVAL PETROLEUM RESERVES/CALIFORNIA, TUPMAN, CA
NRF	NAVAL REACTORS FACILITY, IDAHO FALLS, IDAHO
NTN	NEVADA TEST SITE, MERCURY, NEVADA
NTS	NEVADA TEST SITE, LAWRENCE LIVERMORE NATL LAB, (UC) MERCURY
NVO	NEVADA OPERATIONS OFFICE, LAS VEGAS, NEVADA
NYS	NEW YORK SUPPORT OFFICE, NEW YORK, NY
OGD	OAK RIDGE GASEOUS DIFFUSION PLANT
ORA	OAK RIDGE ASSOCIATED UNIVERSITIES, OAK RIDGE, TN
ORN	OAK RIDGE NATIONAL LABORATORY, OAK RIDGE, TN
ORO	OAK RIDGE OPERATIONS OFFICE, OAK RIDGE, TN
OST	OFFICE OF SCIENTIFIC & TECHNICAL INFORMATION, OAK RIDGE, TN
PAO	PINELLAS AREA OFFICE, ST. PETERSBURG, FLORIDA
PAS	PACIFIC AREA SUPPORT OFFICE, HONOLULU, HAWAII
PDO	PHOENIX DISTRICT OFFICE, PHOENIX, AZ
PEO	PORTSMOUTH ENRICHMENT OFFICE, PIKETON, OHIO
PEP	POSITION ELECTRON PROJECT, STANFORD, CALIFORNIA
PET	PITTSBURGH ENERGY TECHNOLOGY CENTER, PITTSBURGH, PA
PGA	PADUCAH GASEOUS DIFFUSION PLANT, PADUCAH, KENTUCKY
PGD	PORTSMOUTH GASEOUS DIFFUSION PLANT, PIKETON, OHIO
PNJ	PRINCETON AREA OFFICE, PRINCETON, NEW JERSEY
PNL	PACIFIC NORTHWEST LABORATORY, RICHLAND, WA
PNR	PITTSBURGH NAVAL REACTORS OFFICE, WEST HIFFLIN, PA
POO	PORTSMOUTH SITE OFFICE, PIKETON, OHIO
PPA	PANTEX PLANT, AMARILLO, TX
PPF	PINELLAS PLANT, CLEARWATER, FLORIDA
PPP	PRINCETON PLASMA PHYSICS LAB, PRINCETON UNIV., NEW JERSEY

AIM

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Silver Spring, Maryland 20910

301/587-8202

Centimeter

Inches

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2 of 7

CODE	LOCATION DESCRIPTION
PSH	PACIFIC AREA SITE OFFICE, HONOLULU, HAWAII
PSK	PADUCAH SITE OFFICE, PADUCAH, KENTUCKY
PSO	PHILADELPHIA SUPPORT OFFICE, PHILADELPHIA, PA
PSW	PUGET SOUND, SEATTLE, WASHINGTON
PTS	PACIFIC TEST SITE
RAP	REMEDIAL ACTION PROJECTS, GRAND JUNCTION, CO
REH	RADIOBIOLOGY & ENVIRONMENTAL HEALTH LAB (UC) SAN FRAN., CA
RFA	ROCKY FLATS OFFICE, GOLDEN, CO
RFC	ROCKY FLATS PLANT, ROCKY FLATS, CO
RLO	RICHLAND OPERATIONS OFFICE, RICHLAND, WA
RLU	RADIATION LABORATORY (U OF UTAH)
SAO	SACRAMENTO AREA OFFICE, SACRAMENTO, CA
SBO	SANTA BARBARA OPERATIONS
SEI	NATIONAL RENEWABLE ENERGY LAB, GOLDEN, CO
SEP	SOUTHEASTERN POWER ADMINISTRATION, ELBERTON, GEORGIA
SER	NATIONAL RENEWABLE ENERGY LAB, GOLDEN, CO
SFO	SAN FRANCISCO OPERATIONS OFFICE, OAKLAND, CA
SFS	SAN FRANCISCO SUPPORT OFFICE
SLA	STANFORD LINEAR ACCELERATOR CENTER, STANFORD, CA
SLC	SALT LAKE CITY AREA OFFICE, SALT LAKE CITY, UTAH
SNC	SANDIA NATIONAL LAB, LIVERMORE, CA
SNL	SANDIA NATIONAL LAB, ALBUQUERQUE, NM
SNN	SANDIA NATIONAL LAB, NEVADA TEST SITE, MERCURY, NV
SNR	SCHENECTADY NAVAL REACTORS OFFICE, SCHENECTADY, NY
SNT	SANDIA NATIONAL LAB, TONOPAH TEST RANGE, TONOPAH, NV
SOC	SLAC SITE OFFICE, STANFORD, CA
SPJ	SNETTISHAM PROJECT OFFICE, JUNEAU, ALASKA
SPR	STRATEGIC PETROLEUM RESERVE PROJECT OFFICE, NEW ORLEANS, LA
SRA	SNAKE RIVER AREA OFFICE, WALLA WALLA, WASHINGTON
SRD	SAVANNAH RIVER P&L DUPONT, AIKEN, SOUTH CAROLINA
SRE	SAVANNAH RIVER ECOL-UGA, AIKEN, SOUTH CAROLINA
SRO	SAVANNAH RIVER OPERATIONS OFFICE, AIKEN, SC
SSC	SUPER CONDUCTING SUPER COLLIDER, WAXAHACHIE, TX
SSD	SUPER CONDUCTING SUPER COLLIDER, DALLAS
SSR	STANFORD SYNCHROTRON RADIATION LAB, STANFORD CA
STP	STRATEGIC PETROLEUM RESERVE
SWP	SOUTHWESTERN POWER ADMINISTRATION, TULSA, OK
THI	THREE MILE ISLAND PROGRAM OFFICE, MIDDLETOWN, PA
TTR	TONOPAH TEST RANGE, TONOPAH, NV
UBM	U.S. BUREAU OF MINES, IDAHO FALLS, ID
UCH	UC, MERC NV
UCS	UC, SITE 300
UCW	UPPER COLUMBIA, SPOKANE, WASHINGTON
UEP	U.S. EMBASSY, PARIS, FRANCE
UET	U.S. EMBASSY, TOKYO, JAPAN
UGS	U.S. GEOLOGICAL SURVEY, IDAHO FALLS, ID
UMT	URANIUM MILL TAILINGS REMEDIAL ACTION PROJECT OFFICE, AL, NM
VAC	VANCOUVER, WASHINGTON
WAD	WATERTOWN OPERATIONS OFFICE, WATERTOWN, SOUTH DAKOTA
WAP	WESTERN AREA POWER ADMINISTRATION, GOLDEN CO
WFO	WINDSOR FIELD OFFICE, WINDSOR, CT
WIP	WASTE ISOLATION PILOT PLAN PROJECT OFFICE, CARLSBAD, NM

CODE	LOCATION DESCRIPTION
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WMF	WEST MILTON FIELD OFFICE, WEST MILTON, NY
WOB	WO3URN OPERATIONS
WVP	WEST VALLEY PROJECT, WEST VALLEY, NY
YMP	YUCCA MOUNTAIN PROJECT OFFICE, LAS VEGAS, NV
YMS	YUCCA MOUNTAIN SITE, BEATTY, NV
YOR	Y-12 PLANT, OAK RIDGE, TN

18. Audit Locations. Enter the site designation and locations to be visited, if known.
19. Approvals. All indicated signatures must be obtained before the job can be entered into the IGDBMS.

SAMPLE RESPONSE TO REFERRAL FROM INVESTIGATIONS
OR INSPECTIONS (USE MEMORANDUM PAPER)

DATE:

REPLY TO
ATTN OF:

SUBJECT:

TO:

We have noted your referral of (subject and date). The _____ Regional Audit Office has accepted (denied) the subject referral. (If denied, give reasons; if accepted, provide any necessary detail.)

(Name), Manager
_____ Regional Audit Office

AUDIT REQUIREMENTS--FINANCIAL VS. PERFORMANCE

STANDARD OR REQUIREMENT	TYPE OF AUDIT	
	Financial	Performance
GENERAL		
Is a clearly stated objective needed?	Yes	Yes
Do the General Standards of staff qualifications, independence and due professional care apply?	Yes	Yes
Do the AICPA standards apply?	Yes	No
FIELD WORK		
Are there standards for planning, supervision, internal controls, and evidence?	Yes	Yes
Is compliance testing required?	Yes	Yes, to the extent required by the audit objective. ¹
Must audit steps be designed to detect errors, irregularities, and illegal acts? (SAS 53 and SAS 54)	If acts could materially affect balances. ^{1,2}	If such acts could significantly affect audit objective. ^{1,2}
Is a documented understanding of the internal control structure required? (SAS 55)	Yes	Yes, to the extent required by the audit objective. ^{1,3}
REPORTING		
Is a GAGAS statement required?	Yes	Yes
Must the report include the results of tests of compliance?	Yes	If significant or relevant to audit objective
Must all instances of material noncompliance be reported?	Yes	Yes
Should the report include the auditor's understanding of the internal control structure and assessment of control risk?	Yes Yes	Yes, but... ⁴
Should the report include significant weaknesses identified during an assessment of internal controls?	Yes	Yes

1. The audit standards covering compliance testing, review of internal control structures, and design of steps to detect illegal acts are closely intertwined. In each case, the audit objective plays a key role as to the applicability of each standard. While in theory there may be instances in which the audit objective is so narrowly defined that compliance testing may be unnecessary, experience has shown that most audit objectives will involve some degree of compliance testing.

Likewise, most audits will require a review of the applicable internal control structure. Audit steps must also be designed to detect illegal acts when there is reason to do so. One could argue, however, that audit steps relating to compliance testing and internal control structure review are, among other things, designed to detect illegal acts. Generally, such steps are specifically designed to complement a characteristic revealed during the audit that may lead to the discovery of an illegal act. By their very nature, some audit objectives--e.g., determining if bid rigging or money laundering has occurred--will require audit steps designed to detect illegal acts at the start of the audit. Also, some auditors may design audit steps to detect illegal acts at the start of an audit because of their experience in particular audit areas. However, the discovery of a characteristic of an illegal act will more often be the reason an auditor prepares in depth audit steps to determine if an illegal act has occurred.

A characteristic of an illegal act can be almost anything observed during an audit that creates an awareness of possible illegal activities. Such characteristics may be weak internal controls that create an opportunity for illegal acts to occur or a more definitive observation, such as altered payroll records, that indicates illegal activity may have occurred. The discovery of such characteristics may occur at any time during an audit but is most likely to occur during the survey.

2. Auditors must design steps to detect errors, irregularities, and illegal acts that could have a direct and material effect on financial statement balances (financial audit) or significantly affect audit objectives (performance audit) (see Chapter 5). Such steps must be designed in every instance where a characteristic of an illegal act is noted. The generic definition of a characteristic of an illegal act is: An observed internal control weakness, personal behavior, relationship, or deviation in recordkeeping that raises the skepticism about the fidelity of a function in which there is an opportunity for an illegal act to occur.

3. SAS 55, "Consideration of Internal Control Structure in Financial Statement Audits," is not required for performance audits. However, the 3-part process prescribed by SAS 55 is similar to what should be done in any good audit survey. This process involves understanding the internal control structure, assessing risk, and designing appropriate audit steps. For this reason, the concept and approach prescribed by SAS 55 will be adapted and applied to all OA audits, including performance audits to the extent required by the audit objectives.

4. Reporting on internal controls will vary depending on the significance of weaknesses found and their relationship to the audit objectives.

CHAPTER 6CONDUCTING THE AUDITA. SCOPE OF CHAPTER

This chapter sets forth policies and procedures to be followed in conducting and supervising audit fieldwork.

B. INITIATING AN AUDIT

This section sets forth the procedures to be followed in initiating an audit. Specific steps required to start an audit include (1) ensuring that an up-to-date Planned Audit Profile has been submitted, (2) inputting the necessary job-related information to the Inspector General Data Base Management System (IGDBMS), (3) assigning audit staff, (4) sending a "Letter of Notification" to the auditee, (5) ensuring that an audit program has been developed and approved for the assignment, and (6) holding a formal entrance conference.

1. Submitting Planned Audit Profiles. With the exception of certain audits (see section D.6.c.), assignments will not begin until a Planned Audit Profile has been submitted and approved. The format for preparing Planned Audit Profiles is illustrated in chapter 5, exhibit A (A:AM05EXA.WPF).

Regional Offices will submit Planned Audit Profiles for all audits to AP³ at least 4 weeks before the date they plan to start work on the audit. If a Planned Audit Profile was previously submitted as part of the annual audit work plan, it will be reviewed and updated as appropriate. After the Planned Audit Profile is received and approved by AP³, it will be submitted to the DAIG/AO and the AIGA for their review and approval. Approved profiles are to be returned to the Region and AP³ where they will be retained on file as evidence of all approved job starts.

2. IGDBMS Responsibilities. The Inspector General Data Base Management System (IGDBMS) is a primary tool of management to track the progress of audits. Therefore, it is essential that information entered into the IGDBMS is accurate and up-to-date. When Planned Audit Profiles are approved, AP³ is responsible for (1) setting up an IGDBMS job file and (2) notifying the Regional Offices by E-MAIL message that an audit has been approved. At that point, staff can begin charging time to the appropriate job code. The AIC is then responsible for entering the required information into the IGDBMS job file. For example, when notice is received that an audit has been approved, the Region/Field Office should enter into the IGDBMS all additional information required on the "Start" (ISD) screen, information on the "audit objective" (IOB) screen, and data on the "Task Identification" (ITA) screen if required. Exhibit N (A:AM06EXN.WPF) describes responsibilities for maintaining the IGDBMS throughout an audit, and provides instructions for accessing audit tracking reports available through the system.

3. Assigning Staff. Regional Managers are responsible for ensuring that an adequate number of staff with appropriate experience, skills, and

knowledge for the job are assigned to each audit. When appropriate because of geographical location or functional job duties, this responsibility can be delegated to designated ARMs or Audit Directors.

Audits involving the review of general and application controls in computer-based systems, obtaining access to information already on a computer, standardized data collection techniques, or statistical sampling should be coordinated in advance with the Director for Technical Support Staff, AP3, to ensure that the audit team has adequate knowledge, skills or abilities to utilize such techniques and is following approved practices. If AIGA staff with the necessary experience or skills are not available, consideration should be given to obtaining assistance from audit services contractors or consultants. See chapter 8 for more detailed guidelines on computer-related audits and use of quantitative techniques.

4. Notification Letter. Regional Managers have responsibility for sending "Letters of Notification" to an auditee. Normally, this letter should be sent no later than 10 days before the entrance conference and the initiation of audit work. The letter should state the general purpose of the audit and the scope of planned work. Also, a copy of the letter will be provided to AO and AP3. See exhibit A (A:AM06EXA.WPF) for a sample notification letter.

5. Audit Program. As one of their first tasks on an assignment, AICs are responsible for ensuring that an audit program has been developed and approved to address the specific audit objectives. Before auditors start actual fieldwork at an audit site, the audit program for survey or audit verification work is to be reviewed and approved by an Audit Director or ARM.

a. Type of Audit Work Needed - In most cases, a survey will be needed to determine the existence of potential findings which require detailed audit verification. In other cases, potential findings may have already been identified and sufficient information exists for auditors to proceed with detailed audit verification steps. For audits that involve unusual circumstances, regional managers, for good and valid reasons, will be permitted to waive certain policy and procedural requirements in developing and processing audit reports. These unusual circumstances will not circumvent any audit standards. The written waiver will fully support reasons for any changes and become part of the workpaper files. An informational copy of the waiver will be provided to AO.

(1) Survey Work. A survey is intended to be a process for quickly gathering information, without detailed verification, on an auditee's programs, activities, and functions. This information is assembled and analyzed to determine if potential findings exist and to write detailed audit steps. Section D of this chapter provides detailed procedures for performing survey work.

(2) Audit Verification. For some audits, auditors may be able to proceed directly to detailed verification steps where potential findings have already been identified and sufficient information exists for the auditors to determine the nature and extent of additional audit work needed to fully develop findings. Section E of this chapter provides detailed procedures for performing audit verification work.

b. Audit Program Content - A generalized survey program is illustrated in exhibit B (A:AM06EXB.WPF). Audit programs will differ depending on audit objectives, the type of audit being conducted--i.e., financial or performance, the amount of information that is available for planning detailed audit verification steps, and the materiality or significance of expected findings. However, audit programs for both survey and verification work should generally include the following information:

(1) Introduction and Background. Information should be provided about the organization, program, activity, or function to be audited. This information should include a statement of program purposes and goals, standards or plans for the area or issue to be studied.

(2) Objectives and Scope of Audit. The objectives and scope of the audit should be clearly stated or described. The general objective or overall purpose of an audit usually relates to an activity's primary function or mission. More detailed sub-objectives are usually needed to describe specific areas that will be emphasized during the audit. The nature and scope of work planned in order to reach conclusions on the stated objectives should also be described.

(3) Audits Steps/Methodology. The audit program should lay out suggested steps and procedures for developing and supporting all elements of a finding--i.e., criteria, condition, cause, effect, and recommendations--in accordance with audit objectives.

(4) Special Instructions or Responsibilities. The audit program should identify specific staff responsibilities for the audit, particularly if it involves work at multiple locations.

(5) Evidence of Review and Approval. Evidence of supervisory review and approval of a survey program, audit program, or contractor workplan should be documented and retained. This may be accomplished either by using (1) signature blocks incorporated within the audit program or (2) separate cover sheets which reflect review and approval.

c. Approval of Audit Programs - Audit Directors are responsible for reviewing and approving audit programs for both survey and verification work to ensure that the planned scope and methodology of work will satisfy the stated audit objectives and will be performed in accordance with the policies and procedures set forth in this manual. ARMs will review and approve survey or verification programs for more complex audits, major multi-location audits, and all multi-regional audits. Evidence of this supervisory review and approval will be documented and retained with the audit workpapers.

6. Entrance Conference. A formal entrance conference will be held for all audits. An entrance conference is the initial conference held at or near the beginning of the audit with the highest management level of the entity audited. The primary purposes of an entrance conference are to acquaint the auditee with audit objectives and approach, obtain the managers' suggestions for areas needing audit coverage or emphasis, and make administrative arrangements (space, equipment, working hours, etc.).

a. Planning for Conferences - The manner in which a conference is

conducted and the scope of the subject matter to be discussed will be determined by the Regional Manager or his/her designee. All entrance conferences will be coordinated, in advance, with the DAIG/AO, if they involve multi-region audits, audits in which AO has an assigned monitor, or are to be held by ERO or WRO field staff with Headquarter's personnel.

(1) Arrangements for an entrance conference should be made soon after an audit is scheduled. Normally, "Letters of Notification" should refer to the need to schedule an entrance conference, recommend a date and time for the conference, or refer to an entrance conference already scheduled. See exhibit A, A:AM06EXA.WPF, for a sample letter of notification which contains reference to scheduling an entrance conference.

(2) Detailed planning for the conference shall be based on such variables as the objectives of the audit, familiarity of the DOE management representatives with OA's mission and operations, position or level of representatives attending, significance of the audit, and the known desires of the DOE officials.

b. AIGA Representation - The DAIG/AO or a Regional Manager, as appropriate, is responsible for decisions on the number and level of AIGA audit staff that will attend an entrance conference. The knowledge and roles of OA staff, level of representation by the organization being audited, relative significance of the organization, and other similar factors must be considered.

(1) The AIC, Audit Director, and either the Regional Manager or designated ARM should normally attend the entrance conference. Attendance by the Regional Manager or ARM may not be necessary at the start of small or narrowly scoped audits.

(2) Representation by senior OA officials may be desirable at some entrance conferences, such as conferences involving DOE Headquarters personnel or a major multi-location audit, depending on the relative importance and scope of the audit, as well as relationships with and level of DOE officials attending the conference.

c. Conducting the Entrance Conference - The agenda for a conference should be carefully tailored to the requirements of the specific audit, and should consider the following:

- o Opening remarks, including introduction of AIGA audit staff present.
- o A brief overview of OA's mission and organization, and types of audits performed.
- o A description of specific audit objectives, scope, and methodology.
- o Solicitation of management comments regarding significant aspects of the organization, operations, and procedures, with particular emphasis on management initiatives underway (e.g., major reorganization or significant changes in mission) or problems affecting the auditee's operations (e.g., funding shortfalls or personnel shortages) that could affect the audit.

- o Designation by management of primary points of contact or liaison personnel during the audit.
- o The auditee should be informed that the AIC will be available as often as necessary to apprise management of the progress of the audit and of the tentative findings being developed.

d. Record of Entrance Conference - The AIC or other designated person will prepare a memorandum summarizing the highlights of the conference. This memorandum will be made part of the workpapers and will include the names and organizations of all persons attending the conference, disclose any commitments or decisions made, and otherwise summarize the conference results.

C. AUDIT TIMELINESS

To ensure that audit reports are as timely and as useful to management as possible, all audits should generally be completed within specified timeframes. In planning and conducting audits, the maximum number of elapsed days should not exceed 220 for single-site audits, 290 for multi-site audits, or 365 for multi-region audits. In order to meet these overall timeframe limitations, audits should be conducted in accordance with the milestones shown in the following table:

Type of Audit	Audit Phase				
	Entrance Conference	Complete Field Work		Reporting	
		Survey	Audit Verification	Official Draft	Final Report
Single-Site	X	X+65	X+140	X+160	X+220
Multi-Site	X	X+90	X+210	X+230	X+290
Multi-Region	X	X+90	X+285	X+305	X+365

The major phases and related milestones for typical AIGA single-site, multi-site, and multi-region audits are shown in more detail in exhibits C (A:AM06EXC.WPF), D (A:AM06EXD.WPF), and E (A:AM06EXE.WPF). These dates are not intended as rigid guidelines. However, audits should be completed within the maximum prescribed timeframes. The following milestones are particularly significant:

1. Entrance Conference. Although audit planning may begin well in advance of an entrance conference, this date will be used to mark the official beginning of an audit. Not more than 10 percent of total planned staffdays may be expended before the entrance conference is held.

2. Survey Completion. At the end of the survey, the audit team needs to prepare the End of Survey Decision Contract and submit it through channels for the required approvals. There is no requirement that the survey extend for the full amount of time shown in the chart above. Surveys can be, and often are, completed before the target date. The date listed for the end of survey should be used as a deadline for submission of the End of Survey Decision Contract by the Regional Manager. At this time, the data base should be updated to show that the audit is in the verification phase.

3. Complete Audit Verification Work. During the audit verification phase, the audit team has to perform the detailed audit verification steps, ensure that a finding is adequately developed, and obtain required reviews and approvals. A tentative finding and recommendation (TF&R) is normally developed as part of this process, as illustrated in exhibits C, D, and E. However, the development of TF&Rs also initiates the reporting process in that it serves as the initial vehicle for discussing tentative findings with the auditee and obtaining written comments.

4. Issue Official Draft. The official draft report will be issued after management's comments on the TF&R have been received, analyzed and incorporated into the draft report, and referencing of the official draft has been completed.

5. Hold Exit Conference. After comments on the official draft have been received, a formal exit conference should be scheduled.

6. Issue Final Report. Comments received on the official draft or at the exit conference should be analyzed and incorporated into the final report. The final report package should be prepared and the report distributed to the appropriate recipients.

D. PERFORMING SURVEY WORK

In most cases, the audit team will need to perform an audit survey of the auditee in order to identify potential findings and to prepare detailed audit verification steps. Surveys are intended to be a process for quickly gathering information, without detailed verification, on an auditee's programs, activities, and functions, with the purpose of identifying potential findings within the overall objective of the audit. Detailed procedures for performing survey work are provided below. A survey may not be needed on audits where a "GO" decision has already been made, such as for a financial audit. In such cases, the audit program should be designed to enable the auditors to proceed directly to detailed audit verification steps (see Section E of this chapter).

1. Survey Timeframes. Survey work should normally be completed within 65 calendar days after the entrance conference for single-site audits, and within 90 days for multi-site or multi-region audits. Audits are not to be suspended in the survey phase unless prior approval is obtained from the AIGA. Requests for suspension of survey work should be in writing. The AIGA or designee will respond to such requests within 7 working days. All correspondence regarding suspension must be maintained in the workpapers.

2. Initiating Work at Subordinate Activities. The AIC should arrange for a "kick-off" meeting at each subordinate activity level of the organization prior to commencing audit work in the area. The principal purposes of such a meeting are to

- o Introduce AIGA audit staff to responsible activity personnel;
- o Briefly explain the planned scope of work to be performed;

- o Initiate discussions on significant aspects of the activity's operations;
- o Explain how the results of audit work will be reported to the activity; and
- o If appropriate, request a briefing on activity operations and/or a tour of the activity.

3. Obtaining Survey Evidence. A survey is intended to enable auditors to obtain information about the key systems and procedures used by an organization for managing finances and operations, and for evaluating and reporting performance. Auditors should also obtain information about the size and scope of the auditee's activities as well as areas in which there may be internal control weaknesses, uneconomical or inefficient operations, lack of effective goal achievement, or lack of compliance with laws and regulations.

a. Survey Objectives - The survey objectives will normally be to gather and analyze data to determine if potential findings exist and to decide whether a detailed review of a specific area is warranted or possible. To make this type of decision, the survey should be based on an orderly approach to planning and carrying out audit work and for applying scarce auditing resources where they will do the most good. Although a survey program may not contain detailed audit steps, it should contain the same basic structure as discussed in item B.5. above. As an audit progresses, the audit program should be reviewed and refined, as appropriate, in order to update the objectives and to develop detailed verification steps.

b. Survey Methodologies - Common methods of obtaining evidence during a survey include the following:

- o Physical inspections: In most cases, onsite observations are indispensable in helping the auditor to gain a quick working knowledge of an organization's operations and environment.
- o Discussions with agency officials and employees: Various levels of officials and employees within an organization should be contacted to obtain an understanding of their responsibilities and methods of operations. They should be specifically asked about areas that are troublesome or that concern them, but on which they lack reliable information.
- o Interviews with others: Auditors may find it useful to interview concerned or knowledgeable persons outside the organization to obtain indications of program weaknesses.
- o Use of questionnaires: Because numerous interviews could be costly and time consuming, auditors may want to consider the use of questionnaires in selected instances.
- o Reviews of documentation: Auditors should obtain and review the same information that is available to management for its use. If

expected information is not available, the auditor should ask how operations are controlled in the absence of that information. Areas normally worth pursuing include the following:

- Legislation, regulations, executive orders, court decisions, industry standards, and other criteria affecting the auditee's operations should be readily available.
 - Standard operating procedures, mission or function statements, and other written material should be available that documents the auditee's normal operating procedures and critical internal controls.
 - Reading or "Chron" files should be available that document management's current activities and concerns.
 - Management reports (e.g., budgets, operating statements, cost reports, exception reports, etc.) can be useful for making comparisons, highlighting variances, and otherwise understanding how the organization is managed.
 - Prior studies and audit reports should be on file which may provide ideas on problem areas within the organization.
 - Legislative histories, hearings, and proposed legislation may be useful in identifying potential problem areas.
- o **Transaction testing:** Tracing or "walking-through" a few specific work activities from beginning to end may provide useful insights into the organization's operations. However, such testing may be time consuming. Once a weakness is identified, tests to determine the significance or extent of a problem would normally be conducted as part of the detailed work steps in the verification phase.
 - o **Flow charts:** Auditors may find it useful to obtain or prepare flow charts that graphically portray the flow of work and related management control structures.

c. Documenting Work Performed - Auditors are to ensure that their workpapers contain sufficient data to support any judgments or conclusions to be made based on survey results. However, auditors are also expected to use their judgment in terminating work in areas where there appear to be strong internal controls, little risk of noncompliance, or limited opportunity to identify improved economies or efficiencies. More detailed requirements for planning considerations and workpaper preparation are provided in chapters 5 and 7, respectively.

4. Identifying Potential Findings. During a survey, auditors must continually evaluate information obtained to ensure that they are accomplishing survey objectives, identifying potential findings, or determining the nature and extent of additional audit work needed. In general, this can be accomplished by identifying and/or developing as many attributes of a finding

as possible, comparing the condition with the criteria, looking for reasons for the deviation between the condition and criteria, and assessing the potential significance of a finding.

a. Attributes of a Finding - It is important for auditors and supervisors to be consistent in how they evaluate survey information. Therefore, the support for potential findings should be developed in terms of the finding attributes.

(1) Criteria. Criteria tells the reader what should be--i.e., the standard for measuring performance or the goals to be achieved. Examples are laws, regulations, orders, directives, policies, procedures, and management principles or good business practices.

(2) Condition. By definition, an adverse condition ("what is") differs from the criteria ("what should be"). It tells the reader what was found through factual statements. Specific examples and concrete details concerning a reported condition are needed in order to convince a skeptical manager. Emphasis should be placed on discussing accepted management practices and procedures that were either not employed or were not operating properly.

(3) Cause. Cause describes how or why the condition came about and is the reason for the difference between what is and what should be--i.e., why the condition happened. Each finding must include the underlying causes of the conditions reported. The auditor should determine if the cause relates to (1) a lack of procedures/controls, (2) a failure to follow established procedures/controls, (3) a misinterpretation of procedures/controls, or (4) other reasons such as organizational conflicts or resource availability.

For compliance findings, report the the underlying cause(s). State the cause as simply as possible. However, if the cause is complex, explain it in greater detail. Possible causes are not expected to be included.

(4) Effect. Effect tells what resulted from the adverse condition, or "so what," and its significance. Where possible, it should be expressed in quantitative terms--dollars, units of production, etc. Examples include unnecessary expenditures and duplication of effort. However, if the actual effect cannot be determined, comments should be made on the potential effect.

(5) Recommendation. The recommendation describes the action that should be taken to resolve an adverse condition, when, and who should take it. Recommendations in all audit reports should address the underlying causes of the adverse condition. Also, recommendations should logically flow from the causes identified in the finding paragraph. Each cause should be addressed in one or more recommendations. In unusual circumstances, the recommendation may address the condition or effect (e.g. recoup monies stolen).

An analysis of the findings according to the above attributes will usually bring to light any basic problems in developing and organizing audit findings. It will also assist in determining whether all pertinent information was obtained. See exhibit F (A:AM06EXF.WPF) for a worksheet for

developing a finding.

b. Comparing the Condition with the Criteria - Most audit findings originate with comparisons of "what is" (condition) with "what should be" (criteria). When a difference is identified between the two, auditors have taken the first step in identifying an adverse finding. On the other hand, the fact that there is no difference between the condition and the criteria is also significant in terms of satisfying the audit objectives.

c. Assessing the Significance of Findings - Auditors must demonstrate whether an adverse condition found is an isolated example or widespread and the rate or frequency of occurrence. The attention that a finding gets depends largely on its significance, as judged by effect. If possible, this should be stated in quantitative terms, such as dollars, time, or number of transactions. However, intangible effects, such as lowered morale, may also be significant.

d. Explaining Why the Deviation Occurred - The reasons for a deviation between the criteria and condition must be identified and explained. Establishing cause and effect relationships is often the most difficult part of an audit, but is essential in order to identify the basic weakness that allowed a deviation to occur and to design a constructive recommendation.

5. Coordinating With Investigations. Auditors are required to coordinate with the Office of Investigations during the survey. Normally, this may be accomplished by discussing the survey objectives and potential findings with the local on-site investigator or a member of the Headquarters Investigations Division. Such discussions must be documented in the workpapers and will be needed in order to complete the audit Fact Sheet required at the conclusion of the audit (see chapter 11).

6. Reporting Survey Results. At the completion of a survey, the auditor should have gained enough knowledge to clearly identify important issues and problem areas and to decide if and where further audit work is needed. When in-depth work still remains to be done, the auditor should have an idea of what he or she expects to report. Enough information should also have been gathered to allow a detailed audit program to be prepared for conducting audit verification work.

a. Survey Summaries - Generally, formal survey reports will not be required on each survey. However, the AIC is responsible for ensuring that survey work has been appropriately documented, summarized, and crossindexed to the survey program in accordance with the procedures provided in chapter 7 on workpaper support.

b. End of Survey Decision Contract - At the end of most audit surveys, the audit team must have sufficient information to support a decision to either (1) terminate fieldwork and report on information already obtained, or (2) justify the investment of additional resources in order to develop potential findings. The results of this decision will be reflected in an End of Survey Decision Contract.

(1) Format. At the end of each survey, the AIC will be responsible for preparing an End of Survey Decision Contract. The format for this contract is provided in exhibit G (A:AM06EXG.WPF).

(2) Audit Program. Since all audits will normally result in some type of report, a detailed audit program should be prepared that provides the detailed steps for additional audit work that needs to be done in order to develop and verify a finding or otherwise finalize an audit. This audit program should accompany the End of Survey Decision Contract as it is presented for further review.

(3) Refining Audit Objectives. The objectives in the End of Survey Decision Contract need not be precisely the same as those identified in the Planned Audit Profile. Work performed during the survey may have resulted in a refinement of the objectives. Differences, however, must be clearly identified and justified in the contract. Refinement of the objectives at this point is permitted, but not required. Any change in objectives should be entered at the "Objectives" screen in the IGDBMS.

(4) Go/No Go Decisions. The Region should provide the End of Survey Decision Contract to AP3 no later than 30 days after the completion of the survey, or 120 days after the date of the entrance conference, whichever is earlier. Regional Managers are authorized to make Go/No Go decisions for audits which will require less than 250 total staff days. AIGA approval is required for audits needing 250 or more staff days. The "actual survey completion date" entered into the IGDBMS system will be the same date the Contract was signed by the Regional Manager. If a request for extension of survey is needed, the Region should prepare and send the request to AO no later than 120 elapsed days after start of an audit. AP3 is responsible for providing a report to AO of all audits that have over 120 elapsed days but are still in the survey stage.

(5) Responsibilities. An approved End of Survey Decision Contract is a contract between the Regional Manager and the AIGA. A copy of the contract signed by the Regional Manager should be forwarded to AP3. AP3 is responsible for sending the contract to AO and for ensuring that revised staff days and planned dates are reflected in the IGDBMS. AO is responsible for obtaining all approval signatures at the Headquarters level. AO will provide notification and a copy of the approved contract to the Audit Director. AO and the Audit Director will discuss any remarks or changes as they are identified. AO should ensure that AP3 is informed of any changes made to contracts based on AO and AIGA review.

c. Audits Not Requiring End of Survey Decision Contracts. Certain types of audits, such as cost audits and audits required by statute, regulation, or that are administratively imposed, do not require an end of survey contract. For such jobs, Regional Managers are authorized to approve increases of 75 additional staff days and/or 3 additional months to complete from the original planned staff days and completion dates entered into the IGDBMS. The Region should include these changes, together with a rationale, in a memorandum or E-Mail to AP3 which will make the changes to the IGDBMS. These changes should be made within 65 calendar days of the entrance conference. AIGA approval is required for audits needing more than 75 staff days and/or 3 additional months to complete without an End of Survey Decision

Contract.

d. Terminating an Audit - If an audit is terminated prior to completion, the following actions are to be taken:

(1) A letter report should be prepared which summarizes the results of work conducted and conclusions made. See chapter 10 for more detailed guidance on preparing a letter report.

(2) If sufficient audit work has not been performed to support a letter report, then written notice shall be provided to the auditee and other appropriate officials. The letter shall be signed by at least the same level of AIGA official as signed the Letter of Notification. In addition, the AIC (with the concurrence of the Audit Director and the ARM) is to prepare a memorandum for the record that summarizes the results of work conducted and explains why the audit was terminated.

E. PERFORMING VERIFICATION WORK

During the audit verification phase, the audit team is responsible for collecting, analyzing, interpreting, and documenting such information as necessary to accomplish the audit objectives and to support the audit results. This phase of an audit includes direct audit effort, development and staffing of TF&Rs, and required AIGA approvals and consultations. During this phase, the audit team ensures that (1) the attributes of a finding are fully developed, (2) all audit assumptions have been tested and proved or discarded, (3) the workpapers contain sufficient evidence to support findings and conclusions, (4) the workpapers are reviewed by the AIC and other supervisors, (5) supervisory review notes are cleared, and (6) initial management comments are obtained. In general, audits involving detailed verification steps will result in a written audit report.

1. Audit Timeframes. In planning and performing audit verification work, auditors and supervisors need to keep in mind AIGA policies regarding audit timeframes. Although the verification phase of an audit may constitute only a portion of the overall amount of time required to conduct an audit, an excessive overrun during this phase of the audit could cause the maximum elapsed days to be exceeded.

a. Maximum Timeframes - If an audit is expected to exceed maximum elapsed day limitations, the reasons should be set forth in a memorandum from the Regional Manager to the AIGA. This memorandum should also recommend a course of action and provide adequate justification for that recommendation. The AIGA will approve or deny the recommendation and notify the Regional Manager in writing. See section C above for a more detailed discussion of audit timeframe limitations.

b. Audit Suspension - Regional Managers may suspend an audit during the verification phase if audit work is going to be stopped for at least two weeks. Examples of appropriate justification for suspending audit work include

- o higher priority audit work;

- o unavailability of auditor personnel;
- o unavailability of records or auditee personnel; or
- o absence of staff due to illness, injury, or approved annual leave.

If an audit is suspended, the elapsed days will continue to run and staff days will not be charged until the audit is restarted. It is AIGA policy that all audits will be completed within one year. The IGDBMS shall be used to record a suspension and restart of an audit, along with the justification for the suspension. An appropriate justification for suspension must be maintained in the workpapers.

2. Meet With Auditee. If survey work was conducted, the audit team should meet with the auditee to discuss survey results and the scope of additional planned audit work before proceeding with further field work. If no survey work was conducted, then the formal entrance conference will satisfy this requirement. If the audit objectives were refined, refocused, or restated in the End of Survey Decision Contract, and are therefore different from the initial survey objectives, the audit team should inform management of the new objectives at this time.

3. Conduct Detailed Verification Steps. Planned audit steps need to be translated into tasks or work segments that can be assigned to and carried out by individual staff members. As test and verification procedures are conducted, the audit team must ensure that the evidence obtained meets the basic tests of sufficiency, competence, and relevance; that findings and conclusions are based on an objective evaluation of all pertinent facts; and that the audit has been conducted in accordance with prescribed AIGA standards and procedures.

a. Execute Audit Program - Each audit is to be conducted in accordance with an approved audit program (see section B of this chapter). This audit program should serve as a guide for ensuring that the audit is performed in an efficient and effective manner. Audit programs are to be followed, unless significant deviations are justified by the AIC and authorized by the same supervisory levels that approved the original audit program. This requirement also applies to work planned, but not completed. However, auditors should not blindly follow an audit program if the prescribed objectives and audit steps are not resulting in reportable findings or do not otherwise seem to be compatible with actual audit findings. Instead, they are responsible for using their own initiative in determining the appropriateness of steps in the audit program and in assessing the results of the work.

(1) Using Data from Computer-based Systems. Auditors are responsible for following the guidance in chapter 8 to ensure the reliability of data obtained from computer-based systems.

(2) Using Advanced Audit Techniques. If computer-assisted, statistical sampling, or other advanced audit techniques are used, auditors are responsible for following the guidance in chapter 8.

(3) Internal Controls. As discussed in chapter 5, the need to assess internal controls and the focus of that assessment vary with audit

objectives and the type of audit--i.e., financial or performance. However, the basic purpose for evaluating internal controls--i.e., to determine the extent to which existing controls can be relied on in planning and conducting audit verification steps--generally remain the same.

(4) Fraud, Abuse, and Illegal Acts. Auditors are generally not responsible for investigating fraud or other illegal acts. They are, however, responsible for following the procedures established in chapter 5 for developing procedures to assess compliance with laws and regulations. If indications of possible illegal acts do come to their attention, the procedures established in chapter 4 will be followed.

b. Document Work Performed - The AIC is responsible for ensuring that audit work is performed in accordance with the audit program and that workpaper support is obtained and prepared in accordance with the policies and procedures established in chapter 7. However, as a minimum, the workpapers will

- o contain a written audit program cross-indexed to the workpapers, including reasons for audit steps not performed and documentation of audit steps added during the audit;
- o contain the audit objectives, scope, and methodologies;
- o contain summaries and detailed results of audit;
- o contain sufficient information, including the purpose, date sources, and nature of work conducted so supplementary explanations are not required;
- o be legible with adequate indexing and cross-referencing, and include summaries and lead schedules, as appropriate; and
- o restrict information to matters that are materially important and relevant to the objectives of the audit.

Although chapter 7 provides more detailed procedures for preparing workpaper support, the audit team should ensure that it has documented all major decisions and milestones on the audit. Exhibit H (A:AM06EXH.WPF) provides a checklist for tracking documentation of these major decisions and milestones.

c. Analyze and Summarize Audit Evidence - As test and verification procedures are carried out, the audit team must ensure that the evidence obtained meets the basic tests of sufficiency, competence, and relevance. The findings and conclusions must be based on an objective evaluation of all pertinent facts, and the results of this evaluation or analysis must be documented in the workpapers. In addition to the specific audit objectives, particular attention should be paid to analyzing and summarizing the data needed to address the GAO Yellow Book requirements. Specifically, each audit team should prepare workpaper summaries showing their analysis and evaluation of (1) the adequacy of internal controls, (2) compliance with laws and regulations, including indications or instances of illegal acts, and (3) issues needing further study and consideration.

d. Coordinate With Investigations - Auditors are normally required to coordinate with the Office of Investigations during the audit survey. Where no survey is required, this coordination must be accomplished during detailed verification. Auditors should discuss the audit objectives and potential findings with the local on-site investigator or a member of the Headquarters Investigations Division. Such discussions must be documented in the workpapers and will be needed in order to complete the audit Fact Sheet required at the conclusion of the audit (see chapter 11).

4. Develop Tentative Findings and Recommendations. It is OA's policy to develop and staff tentative findings, and obtain management comments as early as possible during an audit, rather than waiting until all field work has been completed and the draft report prepared. TF&Rs should be discussed with the auditee as the attributes of a finding are being developed and before fieldwork is completed. All attributes of a finding must be fully developed for each finding. As previously indicated, exhibit F (A:AM06EXF.WPF) provides a worksheet for developing a finding. Procedures for developing and staffing TF&Rs follow.

a. Format for Tentative Findings - The format for TF&Rs should be consistent with the "Findings and Recommendations" section of Blue and Buff Cover reports described in chapter 10. The TF&R is a "TENTATIVE" document and should not look like a final audit report. Also, TF&Rs will not include sections for management or auditor comments. Prior to issuance, the TF&R should be cross-indexed to the workpapers and the workpapers reviewed as required by chapters 7 and 12. The phrase "TENTATIVE FINDING AND RECOMMENDATION" will be stamped at the top of each page or, alternatively, inserted as a page header.

b. Informal Staffing of Findings - Upon completing reviews of workpapers and the draft TF&R, the AIC should arrange to meet informally with the activity personnel. This initial staffing of the finding should be with personnel at the activity level closest to where the condition prevails or is identified. At the meeting, the AIC should provide the participants an opportunity to read a copy of the draft TF&R in order to identify and correct any misstatements of fact before the TF&R is formally issued. If activity personnel cast doubt on the validity of reported statements or facts, the AIC must make every effort to resolve possible misstatements prior to the TF&R being issued to management. Potential monetary or other benefits, if any, must be included in the discussion.

c. Issuing the TF&R - Following discussions with the responsible operating personnel at the audited activity, and any revisions to the TF&R made necessary by information obtained during the discussions, two copies of the TF&R shall be submitted formally for comments to the level of DOE management responsible for the program or activity. Normally, the TF&Rs are formally issued to DOE management for comments as they are developed throughout the audit. Memoranda transmitting TF&Rs to an Assistant Secretary or equivalent will be signed by the AIGA. As indicated in Chapter 12, TF&Rs subject to AO review must also be submitted to AO prior to being issued.

d. Estimated Monetary Impact - A copy of the "Estimated Monetary Impact of Tentative Finding" form must be presented to management with the TF&R. This allows the DOE managers to consider the potential budgetary impact

of the tentative finding and to plan appropriate budgetary adjustments. The major purposes of the Estimated Monetary Impact form are to: (1) focus attention on potential savings early in the audit and to support savings projections; (2) disclose to management the potential impact of findings; and (3) provide a basis for discussion of the savings and to facilitate reaching agreement with management on the dollar impact of the findings prior to finalization of the report.

The report must include essentially the same information on the estimated impact of a finding as is on the Estimated Monetary Impact this form. This requirement is necessary because the form does not accompany the official draft and final report. The report must also include supporting information, calculations, and other information that readers need to reach the same conclusion the auditors reached. The form and preparation instructions are included as exhibit I (A:AM06EXI.WPF).

e. Transmittal Memorandum - A sample transmittal memorandum for a TF&R is shown in exhibit J (A:AM06EXJ.WPF). Transmittal memoranda should contain

- o an identification of the findings transmitted when multiple submissions are made for an audit;
- o an acknowledgment that the tentative findings have been discussed with operating personnel;
- o a request for the auditee's concurrence or nonconcurrence with the findings and their comments on the accuracy of the facts as presented, conclusions reached, and the reasonableness of the recommendations. Additionally, comments are requested on the estimated dollar impact of the tentative findings and on any corrective action taken or contemplated;
- o a request to provide special handling to avoid premature disclosure outside of DOE, since the tentative findings do not reflect the final position of the OIG; and
- o a request that comments be submitted within 15 working days of the date of the transmittal memorandum.

f. Response Time Allowed - The auditee will be allowed 15 working days to provide written comments to the TF&R. If requested and justified, additional time may be granted to the auditee to provide comments. However, when management has been given ample opportunity to respond, neither the completion of the audit nor the issuance of the draft report shall be delayed because management comments have not been received. If the comments are not received by the time the draft report is to be issued, the report shall state that comments were requested and not received.

5. Discuss Findings With Auditee. It is AIGA policy to fully discuss an audit's findings, conclusions, and recommendations with officials of the organizations or activities being audited and to provide them with ample opportunity to comment on their planned corrective actions. In addition to staffing the TF&R and obtaining written comments from management, this should

be done through periodic meetings with management, at activity exit conferences, and at formal exit conferences.

a. Periodic Meetings with Management - Auditors are encouraged to have frequent communication with management during the audit. Informal meetings should be held with key personnel at the operating level to discuss proposed findings, conclusions, and recommendations.

b. Activity Exit Conferences - At the conclusion of audit work at each site or activity, a conference shall be held with key personnel in the activity to discuss the audit results. If possible, these meetings should occur after the TF&Rs have been fully developed. These discussions will be held to ensure that (1) management agrees with the facts presented, (2) all circumstances contributing to the deficiencies are fully considered, (3) reasons for management disagreements with conclusions and recommendations are determined, and (4) other pertinent factors or information that will put findings into proper perspective are obtained and considered.

c. Formal Exit Conference - An exit conference will be held at the completion of the audit to discuss the audit results and give management an opportunity to provide additional comments on the official draft report and any additional facts that could influence the manner in which the final audit report is presented.

(1) Timing of Conference. The exit conference will be held after the official draft report has been issued and management has provided written comments.

(2) Auditee Representation. The conference should be held with the highest management level of the entity audited. Normally, this will include the highest-level official to whom recommendations are directed or his or her designees.

(3) AIGA Attendance. AIGA representation is required for all exit conferences, except contract audits. This representation will normally include the Regional Manager or an ARM, the Audit Director, and the AIC. Other audit staff should attend if needed to address specific segments of the audit. AO representation is required or desirable for some audits, e.g., at conferences involving high-level DOE officials, major multi-location audits, or particularly complex, technical, or controversial audits.

(4) Record of Exit Conference. The AIC, Audit Director, or other designated person will prepare a memorandum summarizing the highlights of the conference. This memorandum will be made part of the workpapers and will include the names and organizations of all persons attending the conference, disclose any commitments or decisions made, and otherwise summarize the conference results.

F. AUDIT VARIATIONS

In general, the procedures that have been spelled out in this chapter will apply to all audits. However, some adjustments in audit procedures may be necessary for large multi-location audits, for audits performed by audit services contractors, or where there is a need to inform management of matters requiring urgent attention.

1. Multi-Site/Multi-Region Audits. By their very nature, multilocation audits can be complex, requiring communication among a large number of participants and the collection and analysis of large amounts of information. The following procedures are provided to assist in ensuring that the audits are performed in a timely manner, are consistent with an approved audit program, and are otherwise performed in accordance with AIGA standards and procedures.

a. The Regional Manager in the lead region shall designate the Audit Control Point (ACP). The ACP will have day-to-day responsibility for directing or participating in decisions involving the audit, such as approval of the audit program, End of Survey Decision Contract, local TF&Rs, official draft reports, and final audit reports.

b. The ACP is responsible for ensuring the accuracy of reports involving assist or multi-region audit work. As a minimum, the ACP should require assist regions to provide referenced workpaper summaries. However, depending on audit circumstances, the ACP may want to consider other alternatives, such as

- o having all workpapers sent to the lead region for review and so that information used can be referenced to the source documents;
- o sending a copy of draft reports to the assist regions so that they can ensure that information from referenced summaries is used properly and is not taken out of context; or
- o visiting the assist regions to review workpapers used to support findings and conclusions and to meet with the auditee to discuss the draft findings.

2. Contracted Audits. Audit work performed by contract auditors, IPAs, consultants, or other external specialists should be performed in accordance with the same standards and policies that govern work performed by AIGA auditors. To accomplish this objective, work performed by contractors will be controlled and monitored by a Contracting Officer's Representative (COR) and, if appropriate, other designated AIGA staff to ensure that it meets AIGA standards and contract requirements.

a. Contracting Officer's Representative - A COR is a Government employee formally designated to act as an authorized representative of the Contracting Officer for specified functions. In accordance with the requirements established in DOE Order 4200.4A, "Selection, Appointment, and Termination of Appointment of Contracting Officers," issued 8-21-89, each regional office will designate a COR for those contracts covering activity within their respective regions. The COR's duties and responsibilities include

- o Monitoring the contractor's compliance with the terms and conditions of the contract;
- o Keeping the Contracting Officer and the Regional Manager informed of any instances where the contractor has not met contract terms, conditions, deliverables, or schedules;
- o Assisting the contractor in resolving technical differences and ensuring that the Government has met its contract obligations to the contractor;
- o Monitoring the administrative and funds aspects of the contract, to include overall contract costs, general appropriateness of costs charged, travel plans, and progress payments;
- o Assisting the Contracting Officer in contract closeout by attesting to the contractor's completion of required deliverables and services, and providing any records required by the Contracting Officer.

CORs are not authorized to (1) negotiate terms or make arrangements or commitments with the contractor which modify the terms and conditions or scope of work in the contract, nor (2) direct or redirect contract action. These actions can only be done by the Contracting Officer.

b. Other Regional Oversight - Regional Managers are responsible for ensuring that the work performed by contract auditors within their region meets all AIGA standards and prescribed procedures. To accomplish this task, they may designate other regional staff, such as ARMs or designated monitors, to assist the COR or to otherwise perform oversight of contract audit work. These actions will include

- o Assisting the contractor in obtaining administrative support, site access, security clearances, and arranging for entrance or exit conferences;
- o Reviewing work plans or audit programs to ensure that work is adequately planned and does not duplicate other AIGA work;
- o Evaluating survey reports, recommending a Go or No Go decision, and determining the amount of additional work required;
- o Accompanying contract audit staff to selected meetings or briefings, such as entrance or exit conferences;
- o Reviewing and recommending acceptance of workpaper support; and
- o Reviewing audit reports or other deliverables to ensure that they meet AIGA standards and contract requirements.

c. Task Statement on Contractor Lack of Impairments - The Yellow Book requires auditors and audit organizations to be free from impairments to independence. To provide assurance that auditors under contract are free from

such impairments, the following language should be inserted into all contractor tasks:

SPECIAL INSTRUCTIONS

The Contracting Officer and/or the Contracting Officer's Representative, as appropriate, will be provided, as part of the Contractor's Work Plan for this task (or equivalent document), a written statement certifying to the fact that the Contractor (1) is not biased because of its past, present, or currently planned interests (financial, contractual, organizational, professional, or otherwise) which relate to the work under this task, and (2) does not obtain any unfair competitive advantage over other parties by virtue of its performance of this task. The Inspector General is responsible for establishing and maintaining independence so the OIG opinions, conclusions, judgments, and recommendations will be impartial and will be viewed as impartial by others. Audit Support Contractors should consider not only whether they are independent and whether their attributes and beliefs permit them to be independent, but also whether there is anything about their situation which might lead others to question their independence.

d. Contractor Certification - The format for the required certification statement is included as exhibit K (A:AM06EXK.WPF).

3. Management Alerts. Management Alerts are internal documents that may be used to inform DOE managers and officials of matters requiring urgent attention. Normally, Management Alerts are used in lieu of a TF&R and are not to be distributed outside the Department. They should be limited to exceptional cases of immediate urgency so as not to diminish the impact of this reporting mechanism. Management Alerts will only be issued at the AIGA or IG level.

Because a Management Alert is an interim DOE communication, subsequent reporting will be governed by the response to the original recommendations, how the urgent matter was found, and the circumstances under which the Management Alert was issued. Management Alerts must be finalized in a subsequent report or dropped if the facts or conclusions are incorrect.

The usual method for subsequent reporting of a problem included in a Management Alert should be a Blue or Buff Cover report. The Blue or Buff report's Findings and Recommendations section should comment on the actions taken by management subsequent to the Management Alert. In some instances, changed circumstances or new facts submitted by management will affect the need for further reporting. As a minimum, however, a letter report will be issued closing the matter.

a. Transmittal Memoranda - Transmittal memoranda for Management Alerts are sent to the DOE official responsible for the audited activity and are similar to the transmittal memoranda for TF&Rs (e.g., see exhibit L (A:AM06EXL.WPF)).

b. Format - As discussed in exhibit M (A:AM06EXM.WPF), a Management Alert should include the following parts: (1) Introduction, (2) Background, (3) Observations, (4) Recommendations, and (5) Request for Management

Comments. Since a Management Alert normally precedes the completion of all audit verification steps, it should be noted that specific problems are reported as "observations" rather than as "audit findings."

FORMAT FOR LETTER OF NOTIFICATION
(USE MEMORANDUM PAPER)

DATE: Month 00, 199X

REPLY TO

ATTN OF: IG-XX

SUBJECT: Survey of (Subject Matter to be Reviewed)

TO: Department Official (Official in charge of entity or activity to be audited)

The first paragraph should begin at the left margin and state our intent to conduct a survey/audit of the subject area. To the extent known, the offices where the survey/audit work will be concentrated and the field sites to be visited should be specified.

The second paragraph states the general purpose of the audit. The wording should closely parallel the approved Planned Audit Profile.

A third paragraph should provide additional or more specific information about the planned survey/audit. For example, this paragraph could be used to inform the reader that the subject survey is part of a larger OA effort. It should also refer to the need to schedule an entrance conference, recommend a date and time for such a meeting, or refer to an entrance conference already scheduled.

The final paragraph should identify the contractor performing the survey/audit work, if any, and the OA point of contact. The OA contact's telephone number should be listed, and the auditee should be invited to call if there are any questions concerning the survey/audit.

(Signature)

(NAME), Manager

Regional Audit Office
Office of Inspector General

cc: (OA and other department officials
who should be made aware of the audit.)

SAMPLE SURVEY PROGRAM

Note: This sample survey program is intended to provide steps that are applicable to most OA surveys. It provides a basic framework, but should not be used as a complete checklist. Auditors must exercise professional judgment in determining which steps, if any, do not apply to the assignment. Additional steps relating to specific audit objectives must, of course, be added.

I. INTRODUCTION AND BACKGROUND

- A. Document the reasons for undertaking the audit.
- B. Provide information adequate to place the audit in context (program budget, staffing levels, controversy, significance, etc.)

II. AUDIT OBJECTIVES

The objectives should be written as clearly, understandably, and specifically as possible. Time spent writing objectives properly is time well spent. The auditor should normally take objectives directly from an approved Planned Audit Profile. Clearly stated audit objectives become critical when designing audit steps to (1) test for compliance with laws and regulations, (2) detect potentially illegal acts, and (3) review internal controls.

III. SCOPE

- A. Determine and document the audit resources to be used in accomplishing audit objectives.
 - 1. Planned start of audit (use date of official entrance conference) and elapsed days allowed for survey work.
 - 2. Who is performing the audit?
 - a. IG staff (names and regional/audit offices)?
 - b. Contract audit staff
 - 3. Staff days available.
 - 4. Locations to be visited.
- B. Determine the time period, organizations, functions, accounts, documents, etc., to be covered in order to accomplish the audit objectives. For example,
 - o Transactions during FY 1990 to be randomly tested; or
 - o Audit work to be conducted at all procurement offices that process more than 100 contracts per year or contracts with a combined value greater than \$100 million.

IV. AUDIT STEPS/METHODOLOGY

[The following audit steps should be tailored to specific audit objectives, and additional audit steps added as needed.]

A. Background.

1. Obtain an understanding of the auditee's activities and functions relevant to the audit objectives.
2. Document the auditee's organizational structure, through up-to-date organization charts, discussions, etc.
3. Document relevant activities and systems using outlines, flowcharts, transactions flows, etc.
4. Identify key personnel.
5. Obtain a statements of missions, functions, duties, etc., for each organizational element being audited.
6. Determine the major data bases maintained, recurring reports, and any special reports issued during the timeframe being reviewed. Determine the primary users of these data bases, the recipients of the reports, and the expected use of and reliance on the reports.
7. Determine the budget of the major programs supported by the auditee, as well as information on the number, recipient, dollar value, function, duration, and location of contracts awarded or managed, and total value of contract expenditures.
8. Obtain copies of any internal standard operating procedures used by the auditee.
9. Discuss any areas of recent management emphasis or new initiatives which are expected to improve operations.
10. Discuss any external constraints or limitations which affect the auditee's operations.

B. Audit Follow-up.

1. Identify on-going and recently completed (e.g., last 5 years) audits or other related studies performed by groups such as the following.
 - a. GAO
 - b. DOE/OIG (i.e., Audits, Inspections and Investigations)
 - c. Other audit groups (DCAA, State/local, etc.)

2. Follow up on specific audit recommendations and determine the status of corrective actions.
- C. Criteria. Determine and document which laws, regulations, or other criteria are applicable to the auditee and relevant to the audit objectives.
1. Laws, statutes, U.S. Codes, Comptroller General (C.G.) decisions, etc.
 2. OMB Circulars, Federal Acquisition Regulations (FAR), and other regulations
 3. DOE Orders
 4. Other standards and guidelines (e.g., AICPA standards or SASS, FIPS PUBS, etc.)
- D. Compliance with Applicable Laws and Regulations. [See also, SAS 53, 54; Audit Manual, Chapter 5. Detailed guidance is also contained in the GAO publication "Assessing Compliance with Applicable Laws and Regulations."]
1. Discuss the applicable laws and regulations with officials of the audited entity to gain a better understanding of their potential significance to the audit objectives.
 2. Design steps and procedures to test compliance to reasonably assure detection of intentional and nonintentional instances of noncompliance that are material or significant to the audit objectives.
 - a. Determine potential characteristics for this audit .
 - b. Extent of work to identify those characteristics .
 - c. Prepare a workpaper describing any work performed and characteristics of illegal acts noted during the audit. [If any such acts are noted, see chapters 4 and 9 of the Audit Manual.]
- E. Internal Controls. [See also chapter 5 of Manual and SAS 55. Detailed guidance is also contained in the GAO publications "Assessing Internal Controls in Performance Audits" and "Assessing Compliance with Applicable Laws and Regulations."]
1. Assess the auditee's control environment with respect to activities and functions that are relevant in terms of the audit objectives. In particular, assess
 - a. Management's philosophy and operating style.
 - b. The auditee's methods of assigning authority and responsibility.

- c. Management's control methods for monitoring and following up on performance, including internal auditing.
 - d. Personnel policies and practices.
 - e. Any external influences that may have a bearing on internal controls.
2. Assess any portion of the auditee's accounting system that is relevant in terms of the audit objectives. In particular, assess
- a. The effectiveness of the accounting system.
 - b. Relevant activities and systems. Document using outlines, flowcharts, transactions flows, etc.
 - c. The role of key personnel.
3. Assess the auditee's control procedures with respect to activities and functions that are relevant in terms of the audit objectives. General standards for internal controls require (1) reasonable assurance that system objectives will be accomplished, (2) a supportive attitude by managers and employees towards internal controls, (3) competent personnel to accomplish assigned duties, (4) identification and development of control objectives, and (5) efficient and effective control techniques for accomplishing the internal control objectives. Also, where relevant, determine the adequacy of controls for the following specific standards:
- a. Documentation. Internal control systems and all transactions and other significant events are to be clearly documented, and the documentation is to be readily available for examination.
 - b. Recording of transactions and events. Transactions and other significant events are to be promptly recorded and properly classified.
 - c. Execution of transaction and events. Transactions and other significant events are to be authorized and executed only by persons acting within the scope of their authority.
 - d. Separation of duties. Key duties and responsibilities in authorizing, processing, recording, and reviewing transactions should be separated among individuals.
 - e. Supervision. Qualified and continuous supervision is to be provided to ensure that internal control objectives are achieved.

- e. Access to and accountability for resources. Access to resources and records is to be limited to authorized personnel, and accountability for the custody and use of resources is to be assigned and maintained.

F. Risk Assessment.

1. In performing the above steps, you should reach conclusions as to the risk that noncompliance with laws and regulations significant to the audit objectives (1) may have occurred, and (2) was not prevented or detected by the internal controls. Document this assessment in the workpapers.
2. Use the risk assessment as the basis for designing detailed audit steps to achieve the objectives. Greater inherent and control risk generally requires increased testing. [See chapter 5 of Audit Manual.]

G. Assess Data Reliability. [See also chapter 8 of the Manual.]

1. Determine whether computer-processed data are an important or integral part of the audit and whether the data's reliability is crucial to accomplishing the audit objectives. If not, document the rationale in the workpapers and proceed with the next section of the survey program.
2. If computer-processed data are important or integral, and if the data reliability is crucial to accomplishing audit objectives, reliability must be assessed. Depending upon whether general and application controls have been reviewed, a limited review of pertinent controls may be needed.
3. Guidance for performing a limited review is found in the GAO publication Assessing the Reliability of Computer-Processed Data. Based on this guidance, design appropriate review steps to assess the reliability of the computer-processed data. Document all steps and conclusions in the workpapers.

H. Special Instructions.

1. Determine specific staff responsibilities.
2. Obtain agreement from assist regions as to work to be performed, summary due dates, etc.
3. Other special instructions ...

V. APPROVAL

The audit program should contain some indication or documentation that it has been reviewed and approved by the Audit Director and/or ARM.

OVERVIEW: CONDUCTING A SINGLE-SITE AUDIT

A typical breakout of the major phases and related milestones for a single-site audit with a 220-day timeframe is shown below.

LEGEND

<< planning prior to performance, |>-->-->| probable range of date, -->-->--> possible range of date, x specific date

OVERVIEW: CONDUCTING A MULTI-SITE AUDIT

A typical breakout of the major phases and related milestones for a multi-site audit with a 290-day timeframe is shown below.

LEGEND

< planning prior to performance, |-----| probable range of date, + + + + + possible range of date, x specific date

OVERVIEW: CONDUCTING A MULTI-REGION AUDIT

A typical breakout of the major phases and related milestones for a multi-region audit with a 365-day timeframe is shown below.

LEGEND

<< planning prior to performance, |> + + + + | probable range of dates, + + + + possible range of dates, x specific date

WORKSHEET FOR DEVELOPING A FINDING

- A. Potential Finding. (The specific problem that indicates a need for action.)
- B. Brief statements of attributes.
1. Criteria. (What should be--the goals to be achieved.)
 2. Condition. (What is--i.e., statements of fact.)
 3. Cause. (Why it happened--the explanation for the condition and the effect.)
 4. Effect. (The difference between what is and what should be, and its significance.)
 5. Recommendation(s). (Describe what actions we want taken, when, and by which manager(s).)
- C. Discussion. [Summarize argument supporting the finding and give specific examples. Normally, this section provides additional detail about how conclusions were reached by "generalizing" about a number of related specifics or details.]

FORMAT FOR END OF SURVEY DECISION CONTRACT

OFFICE OF THE INSPECTOR GENERAL
ASSISTANT IG FOR AUDITS

END OF SURVEY DECISION CONTRACT

1. AUDIT TITLE:
2. AUDIT ASSIGNMENT NO.:
3. AUDIT STAFF:
 - A. In-House:

HQ Monitor
ARM
AD
AIC
Audit Staff
 - B. Contractor:

HQ Monitor
Technical Director
AIC
Audit Staff
4. GO/NO GO RECOMMENDATION:
5. RATIONALE FOR RECOMMENDATION
6. AUDIT OBJECTIVES
 - A. Original
 - B. Revised (based on survey results) -- Must provide adequate basis for change.
7. POSITIVE RESULTS (State positive results, if any, for original survey objectives).

8. POTENTIAL FINDINGS

A. Title:

Criteria -
 Condition -
 Cause -
 Effect -

ESTIMATED STAFF DAYS REQUIRED:
 ESTIMATED CONTRACTOR COST:

ESTIMATED ELAPSED DAYS:

- B. Continue as needed for each potential finding--i.e., Title, Criteria, Condition, Cause, Effect, and Estimated Staff Days, Elapsed Days, and Contractor Cost.

9. MILESTONE SUMMARY

A. Staff Days and Elapsed Days	Staff Days	Elapsed Days
Days Already Used (as of __/__/__)	_____	_____
Additional Days Required		
- To develop potential findings	_____	_____
- For report processing	_____	_____
Total additional days required	_____	_____
TOTAL CURRENT ESTIMATE	_____	_____
ORIGINAL ESTIMATE	_____	_____
B. Planned Report Completion Date:		
Original Planned Date	_____	_____
Current Planned Date	_____	_____

10. APPROVALS:

AIC or Tech. Dir.	_____	Date _____
Audit Director	_____	Date _____
ARM	_____	Date _____
Regional Manager	_____	Date _____
AO/Monitor	_____	Date _____
DAIG/AO	_____	Date _____
AIGA	_____	Date _____

CHECKLIST FOR JOB FILE CONTENTS

Audit File for _____

Assignment No. _____ Report No. _____

	Check if Completed	Date	W/P Reference
Audit Profile	_____	_____	_____
Task Order/Assignment & Amendments	_____	_____	_____
Notification Letter	_____	_____	_____
Survey Program	_____	_____	_____
Entrance Conference	_____	_____	_____
Work/Task Plan (for Contractor)	_____	_____	_____
End of Survey Decision Contract	_____	_____	_____
Audit Program	_____	_____	_____
Indexed Summary/Outline of Facts	_____	_____	_____
Informal Discussions w/ Auditee	_____	_____	_____
Tent. Findings & Rec. (TF&R)	_____	_____	_____
Trans. Ltr. for TF&R	_____	_____	_____
Org. Comments on TF&R	_____	_____	_____
Fieldwork Completed	_____	_____	_____
Segment Summaries:			
-- Compliance with Laws & Reg.	_____	_____	_____
-- Internal Controls	_____	_____	_____
-- Risk Assessment	_____	_____	_____
-- Assess. of Data Reliability	_____	_____	_____
Indexed Report	_____	_____	_____
Indexed Audit Program	_____	_____	_____
Supervisory Review Notes	_____	_____	_____
Coord. w/OIG Investigations	_____	_____	_____
Referenced Draft Report	_____	_____	_____
& Referencing Comments	_____	_____	_____
Official Draft Report	_____	_____	_____
Trans. Ltr. for Official Draft	_____	_____	_____
Exit Conference	_____	_____	_____
Org. Comments on Official Draft	_____	_____	_____
Report Changes Indexed & Referenced	_____	_____	_____
Final Report	_____	_____	_____
Final Report Package: (Mon. Imp.			
Rpt., Memo. of Exit, Final Rpt.,	_____	_____	_____
Fact Sheet, MIS Rpt., Exec.Sum.)	_____	_____	_____
Contractor W/P's reviewed & O.K.'d	_____	_____	_____
Departmental Position(s)	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____

Comments

ESTIMATED MONETARY IMPACT

TENTATIVE FINDING NO. _____ OF AUDIT ASSIGNMENT NO. _____

1. Title of Audit _____
2. Title of Finding _____
3. Location(s) of Audit _____
4. Estimated Amounts:

		Recurring				Potential
	One	Amount		Total		Budget
	Time	Per Yr.	No.Yrs.	Amount	Total	Impact
						Yes or No
Better Used						
Questioned						

5. Calculation of Savings

6. Discussion of Savings Calculation

7. Management Reaction: Concur _____ Nonconcur _____
Explanation:

INSTRUCTIONS FOR PREPARING THE
ESTIMATED MONETARY IMPACT OF TENTATIVE FINDING

This form is to be prepared and submitted at the time each tentative finding is staffed. The form responds to a DOE management initiative to determine the financial impact of savings resulting from OIG reports and to take immediate action to reprogram the saved amounts or make appropriate budgetary adjustments. The major purposes of the form are to: (1) focus early attention on potential savings early in the audit and to support savings projections; (2) disclose to management the potential impact of findings; and (3) provide a basis for discussion of the savings and to facilitate reaching agreement with management on the dollar impact of the findings prior to finalization of the report. Submission of the forms with each tentative finding is required; however, the audit process and timeframes should not be delayed because management disagrees with the impact of the findings.

The heading shall include the sequence as well as the assignment number. Detailed instructions follow:

1. Title of Audit: Actual title of audit or project assignment.
2. Title of Finding: The verbatim title of the tentative finding.
3. Location(s) of Audit: The geographical location(s) where the audit was actually performed.
4. Estimated Amounts: The following categories are used:
 - o Better Used - Value attributed to the increased efficiency or effectiveness that would result in the future from implementation of the recommendations. Depending on the subject matter of the finding, savings of this type could result in reductions of future years' budgets. Note that "better used" amounts have not been spent.
 - o Questioned - An incurred cost questioned because (1) of alleged violation of a provision in the law, regulation, contract, grant, or cooperative agreement; (2) of inadequate support; (3) it is not allocable to Government work on the basis of benefits received; or (4) the expenditure of funds was unnecessary or unreasonable. Note that "questioned" amounts have been spent.

Savings are shown as one time, recurring, and total. One time savings could be a specific amount of cost incurred that is questioned or the difference between an alternative expenditure of capital funds that would accomplish the same result as a larger capital expenditure.

"Recurring savings" occur when implementation of the recommendation can produce savings in more than one year. The number of years a recurring savings is claimed depends on the nature of the finding, but generally should not exceed 5 years. If the number of years is known, that should be reported. If the number of years is not known the savings years should be identified as "unknown," and the annual amount reported. For example, savings resulting from an improved procedure would normally be limited to

1 year since the number of years realized would probably not be known. On the other hand, savings resulting from capital expenditures, such as for machinery or systems, would normally be projected over the life of the asset, not to exceed 5 years. Recurring plus one-time amounts equal total savings.

Indicate whether the amounts identified have potential budget impact. For example, if a budget line item such as a building was identified as unneeded, there would be a clear budget impact. Conversely, there would probably not be a budget impact if a less expensive source of laboratory supplies was identified.

5. Calculations of Savings: The details of the computations made to arrive at the estimated amount of savings will be shown in this section. The details should include the period of time over which savings are calculated. The cost of implementing the recommendations and the savings reduced by such amount should be appropriately considered. Care should be taken to assure that the savings reported in a multi-region report do not duplicate savings reported in regional reports. Attachments to the form may be used if necessary.
6. Discussion of Savings Calculation: The rationale, assumptions, statistical or actuarial analyses, and other mathematical techniques used to calculate savings will be identified in this section along with the supportable raw data used.
7. Management Reaction: This section should identify whether management did or did not concur with savings calculations, and explain the reasons for any management disagreements.

EXAMPLE: TRANSMITTAL MEMORANDUM FOR TF&R
FOR BLUE COVER OR BUFF COVER REPORT
(USE MEMORANDUM PAPER)

DATE: Month XX, 199X

REPLY TO
ATTN OF: IG-XX

SUBJECT: Tentative Finding and Recommendation(s) on "Name of Audit"

TO: Auditee

Attached for your review and comment is a copy of our tentative finding and recommendations on the subject audit. The audit was performed at (location). We discussed the results of the audit with (position title) in (Month, 199x). A copy of the related Estimated Monetary Impact of the finding is also attached.

Please review the information in this finding, and provide written comments within 15 working days on the facts presented, conclusions reached, appropriateness of the recommendations, and reasonableness of the estimated potential monetary impact or other benefits that may be realized upon implementing the recommendations. If you agree with the recommendations, please outline the corrective actions taken or planned, as well as the actual or target dates for the actions. Also include any alternatives to our recommendations if you believe there are better ways to solve the problems discussed in the tentative finding. If you submit alternatives, please include your estimate of the potential benefits to be realized from these alternative actions, and target dates for completing them.

Since the tentative results of audit are subject to change and therefore do not represent the final position of the Office of Inspector General, the contents shall be safeguarded at all times to prevent improper disclosure. According to DOE Order 2320.2B, recipients of tentative findings will only provide the contents to personnel within the Department for official review and comment. The tentative findings and recommendations shall not be provided to anyone outside the Department without the express approval of the Inspector General. In this context, management and operating contractors shall be considered to be part of the Department. However, when tentative findings and recommendations are given to a management and operating contractor, the providing program official is responsible for ensuring that the document is properly safeguarded. The contractors may only receive the tentative finding and recommendations for the exclusive purpose of aiding DOE in the deliberative process. Further, there is to be no premature release to anyone outside the Department. DOE Order 2320.2B also states that all copies of tentative findings and recommendations remain the property of the Office of Inspector General and shall be returned on demand.

Your cooperation will be greatly appreciated. If you have any questions please contact either (Assistant Regional Manager or Audit Director) at (000) 123-4567.

(Name), Manager

Regional Audit Office
Office of Inspector General

Attachment

[Note: TF&R transmittals to an assistant secretary are signed by the AIGA.]

cc:

Statement on Independence and Conflict of Interest

_____ hereby certifies that, to the best of its knowledge, no impairment of independence or conflict of interest, either actual or perceived, exists in performance of task _____. If, after the audit has commenced, any independence impairment or conflict of interest, actual or perceived, are identified, they will be brought to the attention of the Office of Inspector General, in writing, immediately.

Officer/Partner Signature

Date

EXAMPLE OF TRANSMITTAL MEMORANDUM FOR
MANAGEMENT ALERT
(USE MEMORANDUM PAPER)

DATE: Month 1, 199X

REPLY TO
ATTN OF: IG-30

SUBJECT: Management Alert on "Title of Alert"

Attached is a copy of the subject management alert. Although the matters discussed in this document have not been fully coordinated with management, the information is being conveyed at this time because of the need for prompt management action.

We concluded that ...

Please furnish your comments on the factual accuracy of the information and your specific concurrence or nonconcurrence with the recommendations within 15 working days of this memorandum. In addition, we would appreciate being informed of any corrective actions already taken or planned regarding this management alert.

Since our position in the management alert is subject to change and therefore does not represent the final position of the Office of Inspector General, the contents shall be safeguarded at all times to prevent improper disclosure. Recipients of management alerts will only provide the contents to personnel within the Department for official review and comment. The management alert shall not be provided to anyone outside the Department without the express approval of the Inspector General. In this context, management and operating contractors shall be considered to be part of the Department. However, when management alerts are given to a management and operating contractor, the providing program official is responsible for ensuring that the document is properly safeguarded. The contractors may only receive the management alert for the exclusive purpose of aiding DOE in the deliberative process. Further, there is to be no premature release to anyone outside of the Department. The management alert remains the property of the Office of Inspector General and shall be returned on demand.

Your assistance and cooperation are greatly appreciated.

John C. Layton
Inspector General

Attachment

cc:

EXAMPLE OF MANAGEMENT ALERT BODY

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL

TITLE OF ALERT, ALL CAPITAL LETTERS
SINGLE SPACED
CENTERED ON THE PAGE AND UNDERLINED

INTRODUCTION

This section should briefly state the condition which warrants a management alert. It should be kept short because it is not intended to summarize the entire report.

BACKGROUND

This section includes any background information necessary to understand issues discussed in the management alert. It may include such general information as a description of a system or procedure, responsibilities of the organization managing the activity, and specifics on past actions.

OBSERVATIONS

This section includes the condition or conditions requiring the management alert. Specific problems now existing, the need for urgent management action, and the magnitude of the problems in terms of dollars or hazard effects should be discussed.

RECOMMENDATION

The recommendations should specify actions that need to be taken promptly to eliminate or reduce the adverse effects of the problem(s). Begin each recommendation with an imperative verb.

REQUEST FOR MANAGEMENT COMMENTS

This section should ask for written comments that include a statement of concurrence or nonconcurrence and any actions taken or proposed. It should request that the comments be provided within 15 working days on (1) the accuracy of the information presented, (2) agreement or disagreement regarding the recommendations, and (3) action taken or proposed regarding the matters contained herein. It should also state that the contents of the report, along with management's comments, may later be included in a report subject to formal reply requirements.

IGDBMS RESPONSIBILITIES AND REPORTSRESPONSIBILITIES FOR KEEPING IGDBMS CURRENT AND ACCURATE

The Auditor-in-Charge (AIC) and the Technical Director (TD), for contractor performed audits, have the primary responsibility for keeping the information in the IGDBMS current and accurate for each audit (project). This is accomplished as follows:

Both Headquarters and Field elements of the Office of Audits are responsible for entering selected information into the Audit module of the IGDBMS, and to ensure that the information is current. Because reports run at Headquarters and in the Regions depend on the accuracy of information in the system, it is imperative that it be kept current. The following discussion outlines these responsibilities.

As discussed in Chapter 6, the first stage of the audit process requires the Field to submit a job proposal (profile) to Headquarters for approval. Once the Directors of AP3 and AO approve the profile, AP3 is responsible for assigning the audit number, entering the number along with data contained on the profile into the IGDBMS, and notifying the appropriate Region and Office of the new number. At that point, staff can begin charging time to the audit.

When notice is received that an audit number has been assigned and added to the IGDBMS, the Region/Field Office should enter:

- all additional information required on the 'Start' (ISD) screen,
- all additional information required on the 'Milestone' (IML) screen,
- information on the 'Audit Objective' (IOB) screen,
- information on the 'Audit Tracking Code' (ATC) screen, and
- information on the 'Task Identification' (ITA) screen if required.

The Region/Field Office should continually monitor the status of audits, even if actual audit work has not begun, and revise the entrance conference, survey completion, and report milestone dates as appropriate. Since there is no limitation to the number of times a milestone may be revised, all audits should be reviewed bi-weekly, and updated as necessary. Keep the "revised" date column of the IGDBMS current. The dates show what our latest expectations are as opposed to what is shown in the "planned" date column. While an audit is in suspense, enter a remark every two weeks commenting on when to expect the audit to be reactivated, why the audit is remaining in suspense, and if appropriate what is being done to assure that the audit will be reactivated as soon as possible. When the audit is removed from suspense, update the "revised" dates. This information, along with the remarks, is essential if audit management is to use the IGDBMS to keep abreast of the status of the audits.

As Headquarters identifies audits that it intends to monitor, AO, or AP3 in the case of ADP audits not run out of Headquarters, will enter the identity of the Headquarters monitor.

Once the audit begins, the Region/Field Office should enter the 'Actual Milestone' dates as they occur. As discussed in Chapter 6, a copy of the End of Survey Decision Contract is sent to AP3. The date the contract is sent to Headquarters should be entered as the 'Actual Survey Completion' date. When the contract is received in Headquarters, AP3 will immediately update the 'Planned Report Completion Date' and the total number of 'Planned Staff Days' based on the contract.

For those audits not requiring an End of Survey Decision Contract, but where additional staff days or time are found to be necessary, an E-mail message or a memorandum should be sent to AP3 including the changes and providing the rationale for the changes. These changes should be made within 65 calendar days of the audit's entrance conference. AP3 will immediately update the information in the IGDBMS, subject to concurrence by AO. AIGA approval is required where 75 or more additional staff days are required or 3 or more additional months are needed to complete the assignment.

Once the survey has been completed, planned milestone dates for issuing TF&R's, the draft report, and holding the exit conference should be entered by the Region/Field Office. All 'Actual' dates should be entered when the event occurs. However, any changes to Actual Milestone Dates entered by the Region/Field Office can only be made by AP3 after receipt of a written request from the regional office (E-mail or memorandum) with an explanation of the requested change. All requests for changes to an Actual Milestone Date are subject to AIGA approval.

Whenever a change occurs, information on the Audit input screens should be updated. For instance if the objective of the audit changes based on survey results, the information on the 'Audit Objective' screen should be adjusted accordingly.

When any significant event occurs in the audit, remarks should be entered in the 'Audit History' (AHS) screen. This provides a way of tracking audit events for future reference. Anyone in the Office of Audits may enter a remark in the Audit History screen for any audit. Each week, if a remark has not already been entered, enter a remark describing the current status for the audit (progress; actual or anticipated problems; how the problems will be overcome; descriptions of results of special events of the week such as meetings, change in staffing, new TF&R's, supervisory visits and decisions made as a result of the visits; planned future events; etc.). The goal is to keep management advised of the status of the audit through the remarks.

Once the Draft Report has been issued, the Region/Field Office must enter information into the 'Audit Findings' (IFN) screen. This information may be changed if findings change subsequent to the issuance of the Draft Report. Upon issuance of the final Audit Report, the Region/Field Office must enter summary information in the 'Report Summary' (IRS) screen and enter keywords associated with the audit in the 'Index' (IDX) screen.

The entering of information related to IPA contracts or tasks is primarily the responsibility of the Contracting Officers Representative (COR) for each respective contract. Once information on a new contract is entered into the 'Contractor Identification' (ICR) screen by AP3, the COR will take over all other input and update responsibilities associated with the contract, which includes information required in the 'Contract Identification' (ICT) screen, the 'Task Identification' (ITA) screen, and the 'Contractor Time/Cost' (ITC) screen. The COR is responsible for ensuring that the initial task order information is entered in the system. Information should be updated whenever a contract modification occurs, as soon as tasks are assigned, and as soon after receipt and verification of the contractors invoices as possible.

It is also the responsibility of the Region/Field Office to terminate ongoing audits or cancel planned audits that will not be started. This is done by entering a date in the 'Actual Completed with Report' field of the 'Milestone' screen. You will then be prompted to make an entry in the 'How Completed' field. Acceptable entries are "C" for cancelled or "T" for terminated. (When the audit is completed with a report, you will enter "R".)

In addition, the office secretary, ARM, AD, and Headquarters monitor have responsibilities for keeping the IGDBMS current and accurate.

- o the secretary for each office enters into the IGDBMS the time charged to each audit or other project codes as shown on the bi-weekly time sheets.
- o On Monday of each week, the responsible AD and ARM for each audit, obtain and review the Audit Project Summary (APS) Reports to make sure that the reported data is current and accurate and to determine the status of each audit. This practice demonstrates management's interest in and use of the information and serves as a quality control check.
- o Every two weeks, Headquarters monitors will review the data in the system. The monitor is to call the AIC to discuss any corrections needed. The monitor will enter the results of this review in the system.

IGDBMS REPORTS

At the present time, there are ten reports available in the Audit Tracking System of the IGDBMS. Additional reports are being developed and should be available to Audit users in the near future.

Reports can be executed through menu selections and by responding to a few prompts. To get to the Report menu after logging on to the IGDBMS, type 'DBM' at the first menu, followed by 'AUD' and 'RPT'. The reports are run on-line, meaning that the reports will always reflect the most up-to-date data in the system.

All reports can be downloaded to your PC for printing. In fact, seven of the ten available reports will automatically be saved to your DEFAULT account. In addition, all reports can be captured to your PC using the F7 key to toggle the capture feature on or off. Most reports can also be printed as the information is displayed on your monitor by using the <SHIFT>/F2 option. However, you should note that only reports that are downloaded for printing will have the proper page breaks.

CAUTION: Several of the reports that have an LIS extension (APO, CCS, and TCA reports) use only one name for the files that are created. If you run more than one of a particular report (e.g. one TCA report for the Chicago Office and one for the Oak Ridge Office) the system will give them the same name but a different version number. In this case the files might be called AUD_TCA.LIS1 and AUD_TCA.LIS2.

In order to download both files at the same time and not have one overwrite the other, you should type AUD_TCA.LIS.* when you are prompted for the name of the file to download. After you have selected KERMIT and DOWNLOAD you will be prompted for the name you want the downloaded file to have. At this prompt, type /R, then hit return. The system will automatically give each report a different name as it is downloaded to your Default account. Up to five identically named reports can be downloaded at one time using this procedure.

When you download the report to your PC and bring it up as an Enable word processing file, you will be told that the report is in some format other than Enable. Select ASCII and hit <ENTER>. You will then be told that the report will extend beyond your margin. Once again hit <ENTER> and the report will be displayed. For all reports not requiring landscape printing, you should then set your right margin at 80 and your print size at 12 pitch (elite). For those reports that must be printed landscape, the right margin should be set at 170 and the print size at compressed.

Following is a brief discussion of the information contained in each report, suggestions for the best (or quickest) way to print the report, and the file name the report will have when it is downloaded to your PC.

APS - Audit Project Summary Report-Single Audit

This report provides detailed information for a single Audit Number, including:

Milestone dates; Audit codes and descriptions; Task order number and supporting cost and time information for the task; Identification of senior personnel associated with the audit; ATC, facility and location information; Time charged by individual and by the contractor; Staff days planned and used; Elapsed days planned and used; and Report number for audits completed with a report.

For audits completed with a report, the Audit Report - Summary (ARS) Report (see below) will also be produced automatically.

You may also request that the Audit Objective and/or the Audit History (either the last comment only, comments made in the last 30 days, or all comments on the audit) be run along with the APS report.

After you have viewed the requested information, you will be notified that the report is in your personal (default) account on the system, and that the Report Number will be the Audit Number followed by .APS.

This report may be captured or downloaded to your PC for printing, or you may print the report using the <SHIFT>/F2 feature.

APO - Audit Project Summary Report-Single Office

This report provides the same information as the APS report, except the selection criteria is the Audit Office Code, not the Audit Number. An APS-type report will be produced for all OPEN Audits in the selected office.

After the initial file is created, you will be prompted to reenter the Office Code if you want to include the Audit History text (last remark only) with the report. The APO report will be named AUD APO.LIS, and the Audit History report, if requested, will be named A.APO, where the first two characters are the first two letters of the Office Code (e.g. CH for Chicago or LL for Lawrence Livermore).

Although the <SHIFT>/F2 may work in some cases, this report works best if it is captured or downloaded to the PC for printing.

CCS - Audit Contract Cost Summary Report

This report identifies all Task Orders associated with the selected Contract. Enter the two character Contract Code at the prompt. The report will list the following information:

Contractor name; Contract code, number, effective date, and authorized amount; Amount obligated; Project Number, task number and title of all tasks; and Amount authorized, costs/fees incurred and remaining balance for each task, with contract totals also displayed for each of the three amounts.

Contract codes for the current and some previous contracts are:

	Current	Previous
--	---------	----------

ADC, Ltd.	XQ	XP
Cotton & Co.		CG
Irving Burton & Assoc.	VG	VF
Peat, Marwick & Main	MT	MQ
KPMG Peat Marwick	KP	

After you have viewed the requested information, you will be notified that the report is in your personal (default) account on the system, and that the report name AUD_CCS.LIS.

This report may be downloaded to your PC for printing, or you may print the report using the <SHIFT>/F2 feature.

ECR - Open Audits Having an Actual Entrance Conference Date During a Specified Period of Time

This report lists open audits that have an 'Actual Entrance Conference Date' in a specified date range. You will be prompted to enter a Region or Office Code, then the earliest date you want included in the search, followed by the latest date to be included.

Information contained in this report includes:

Audit Number and Title; Actual Entrance Conference and Planned Completion Dates for each audit; Current Status; Last pay period time was charged to the audit by IG personnel; Planned and Actual staff days and elapsed days; and The number of days the audit has been suspended.

This report must be downloaded and printed in compressed landscape mode. The report will be named A.ECR, where the first two characters are the first two letters of the Office Code (e.g. CH for Chicago or LL for Lawrence Livermore) or the Region Code (e.g. CR for Capital Region).

ACD - Audits Completed During A Specified Time Period

This report lists completed audits that have an 'Actual Completion Date' in a specified date range. A completed audit is one that has been 'Completed with a Report', 'Terminated', or 'Cancelled'. You will be prompted to enter a Region or Office Code, then the earliest date you want included in the search, followed by the latest date to be included.

This report includes the same data elements described in the ECR report above, and must be downloaded and printed in compressed landscape mode. The report will be named A.ACD, where the first two characters are the first two letters of the Office Code (e.g. CH for Chicago or LL for Lawrence Livermore) or the Region Code (e.g. CR for Capital Region).

AOR - Audit Objective Report

This report lists the entire text of the 'Audit Objective' as recorded in the IGDBMS. You will be prompted for an Audit Number. After you have viewed the requested information, you will be prompted to enter a 'Y' if you want to be able to download the report to your default account. The Report Number will be the Audit Number followed by .AOR.

You may choose to capture or download this report to your PC for printing, print the report using the <SHIFT>/F2 feature, or simply do a <PRINT SCREEN>.

AHS - Audit History Report

This report lists all remarks entered in the Audit History for a single project. The oldest remark is listed first. After you have viewed the requested information, you will be prompted to enter a 'Y' if you want to be able to download the report to your default account. The Report Number will be the Audit Number followed by .AHS.

Although the <SHIFT>/F2 may work in some cases, this report works best if it is downloaded to the PC for printing.

ARS - Audit Report Summary

This report lists the entire text of the Report Summary for a single project. After you have viewed the requested information, you will be prompted to enter a 'Y' if you want to be able to download the report to your default account. The Report Number will be the Audit Number followed by .ARS.

You may choose to download this report to your PC for printing, print the report using the <SHIFT>/F2 feature, or simply do a <PRINT SCREEN>.

TCA - Time Charged After Audit Completion

This report lists audits that have had time charged to them subsequent to completion. Any time charged during the current fiscal year to an audit more than 14 days after an actual completion date (either by report, termination, or cancellation) has been entered will be reflected on this report. You may select to run this report by Region, Office, or for all Office of Audits.

The following information is included on this report:

Region and Office; Audit Number, Title and completion date; The date time was last charged; and The number of additional hours charged this fiscal year along with the total number of hours charged to the Audit.

This report is automatically saved to your Default account. You may choose to download this report to your PC for printing, or print the report using the <SHIFT>/F2 feature. The file name for the downloaded report will be AUD_TCA.LIS.

PLN - Report of Audits Planned but Not Yet Started

This report lists all audits that are planned (e.g. approved and added to the IGDBMS) but have not yet started. Information on this report includes:

Region; Office; Audit Number; Title of the Audit; Planned Entrance Conference and Completion Dates; Planned Staff Days; and The number of hours charged to the audit, if applicable.

There is no selection criteria for this report - all planned audits will be listed in Office Code order.

This report is automatically saved to your Default account with the name AUD_PLN.LIS. You may choose to download this report to your PC for printing, or print the report using the <SHIFT>/F2 feature.

CHAPTER 7WORKPAPER SUPPORTA. SCOPE OF CHAPTER

This chapter sets forth the policies and practices for the preparation and review of workpaper support for AIGA audits.

B. POLICY AND STANDARDS

A written record of the auditors' work is to be retained in the form of "workpapers" for all OA audit work. These workpapers are the link between fieldwork and the audit report. They are necessary to provide a systematic record of work performed, to assist staff members in pulling ideas together for reporting, and to provide a record (audit trail) of information and evidence supporting the findings, conclusions, and recommendations contained in a report. In addition, supervisors can evaluate workpapers to determine job progress, obtain information for planning and carrying out subsequent jobs of a similar nature, and ensure that audit findings and conclusions are supported by sufficient, competent, and relevant evidence.

1. General Standards. In accordance with GAO and AICPA standards, workpapers prepared to support AIGA audits shall contain sufficient, competent, and relevant data to support findings, judgments, and conclusions reported regarding an organization, program, activity, or function under audit. In preparing workpapers, auditors shall exercise care to ensure that they comply with the following standards:

a. Completeness and Accuracy - Workpapers are to be complete and accurate in order to provide proper support for findings, judgments, and conclusions, and to enable demonstration of the nature and scope of the work conducted.

b. Clarity and Understandability - Workpapers should contain sufficient information and be structured so that supplementary oral explanations are not required. Although conciseness and avoidance of excessive detail is important, clarity and completeness should not be sacrificed just to save time or paper.

c. Legibility and Neatness - Workpapers must be neat and legible to be useful. They should be typed or written neatly at the outset and rewritten only as necessary.

d. Relevance - Workpapers are to be restricted to matters that are relevant to the assignment objectives.

e. Custody and Retention - All relevant workpapers developed during an audit must be preserved and safeguarded in the workpaper files for a time sufficient to meet legal and administrative requirements.

2. Types of Evidence. In collecting workpaper support, auditors shall attempt to obtain the "best" evidence possible in terms of supporting a finding or issue. The various types of information obtained normally include the following:

a. Testimonial evidence consists of statements received from others, such as through interviews, conferences or telephone conversations.

b. Physical evidence includes that obtained by direct inspection or observation of (1) activities of people, (2) property, or (3) events. Such evidence is to be documented by memoranda of observations, photographs, charts, maps, or actual samples.

c. Documentary evidence consists of written records, such as letters, accounting records, invoices, official correspondence, contracts, reports, and management information on performance.

d. Analytical evidence includes computations, statistical summaries, lead schedules, comparisons, reasoning, and separation of information into components.

3. Tests of Evidence. To ensure that the various types of evidence obtained are sufficient, relevant, and competent, the auditors must ensure that the evidence is obtained from a reliable source and is accurate.

a. Sufficiency - Sufficiency is the presence of enough factual and convincing evidence to support our findings and conclusions. When appropriate, statistical methods may be used to establish sufficiency.

b. Relevance - Any information used to prove or disprove an issue must bear a logical, sensible relationship to that issue.

c. Competence - To be competent, evidence should be valid and reliable. Auditors should carefully consider whether reasons exist to doubt the completeness or validity of evidence. The following have been offered as guides for determining competent evidence.

- o Evidence obtained from an independent source provides greater assurance of reliability than that secured from the auditee.
- o Evidence developed under a good system of internal control is more likely to be reliable than that obtained where such control is weak or unsatisfactory.
- o Evidence obtained by the auditor through physical examination, observation, computation, and inspection is more reliable than evidence obtained indirectly.
- o Original documents are more reliable than copies (e.g., a copy of a letter in a sender's file may not be the same as the letter actually sent).

C. WORKPAPER PREPARATION

Auditors, both AIGA and contract, should follow these procedures and guidelines in preparing and reviewing workpapers.

1. Physical Characteristics of Workpapers. Specific physical requirements for workpapers are as follows:

a. Size - Normally, workpapers are to be prepared on standard-sized (8½ x 11 inch) paper. However, large-size documents, computer diskettes and tapes, and physical items or samples may be retained in the workpapers if they represent the best evidence available.

b. Headings - Each workpaper is to contain descriptive headings in addition to the information constituting the body of the workpaper. The workpapers should contain sufficient information to clearly identify the audit and the nature of the data in the workpaper. As a minimum, the workpaper should include the audit assignment number, the name of the program or activity being audited, and the subject and/or purpose of the workpaper.

c. Indexing - Each workpaper will contain an index number for filing and reference purposes. It will also contain a "legend" to explain the meaning of any tick marks or other symbols used on the workpaper.

d. Sources - All workpapers should specifically identify the source of information in sufficient detail that others can evaluate the source and trace the information back to that source. For example, the names of persons contacted to obtain information should be included, as well as their title, room number, and telephone number. In most cases, it is preferable to show both the originator of a document as well as the source from which the auditor obtained the information. Also, the workpaper should be initialed/signed and dated by the auditor preparing the workpaper.

e. Layout of Workpaper - Workpapers must not be crowded. Auditors should leave sufficient space, particularly on summaries and lead schedules, for cross-indexes, footnotes, relevant conclusions and modifications, source statements, and legends for tracing to source and verifying computations.

f. Cover Sheets - Each workpaper bundle shall have a cover information sheet with agency/office, title, location of audit, date, project control number, bundle number, and retention period. See exhibit A (A:AM07EXA.WPF) for a sample cover sheet.

2. Documenting Work Performed. The results of meetings, interviews, conferences, phone calls, etc., should be carefully recorded in the workpapers. This includes liaison visits, overall entrance and exit conferences, and entrance and exit conferences on audit segments.

a. Exhibit B (A:AM07EXB.WPF) illustrates an acceptable format to be followed for interview writeups and offers suggestions on how to conduct interviews. All interview writeups are to include the following information:

- o Name, position, and office of official(s) interviewed.
- o Names of the AIGA staff members present.
- o Date, time, and place of the interview.
- o Purpose and nature of subjects discussed in the interview.

b. Information received over the telephone is to be annotated with the date and time of conversation, and the name, position, and office of the official telephoned.

c. Oral evidence should be verified. If incorrect statements by agency officials are identified, the incorrect statements should be identified by footnote and cross-indexed to the correct facts.

d. If information is particularly significant to an audit, the person interviewed should be asked to read an interview writeup, make any changes deemed necessary, and initial or sign it to show his or her concurrence. If he or she refuses to sign it, it is unlikely much reliance should be placed on the statement in a report.

e. When it is necessary to get especially critical or sensitive information from an interviewee, two auditors should attend the meeting, and both should initial/sign the interview writeup to show their agreement on the accuracy of the writeup.

3. Workpaper Summaries. Where multiple items of information are needed to support a particular finding or conclusion, the auditor should normally prepare a workpaper summary to tie together the evidence relating to a particular topic. Such a summary should assist the auditor in forcing timely analysis of the evidence, identification of additional work needed, and an evaluation of reporting approaches. A workpaper summary would typically include the following:

- a. Objective (Purpose) - Clear statement of the purpose of the summary.
- b. Work Performed (Scope) - A description of the work performed which serves as a basis for the findings (interviews, observations, etc.).
- c. Results (Findings) - A factual summary of the evidence and its source (should not include conclusions drawn from the evidence).
- d. Conclusions - An analytical summary of the facts as they pertain to the issue being discussed (includes a statement of the problem).
- e. Recommendations - What needs to be done to correct the problems noted.

Exhibit C (A:AM07EXC.WPF) provides an acceptable format for a workpaper summary. As information is summarized, it is advisable to discuss potential findings and conclusions with the auditee to ensure that all pertinent facts have been obtained or that there is not another reasonable interpretation to

the data being analyzed. In addition to assisting auditors in verifying the facts obtained, these discussions will also assist in efforts to determine the causes of problems. All summaries will be cross-indexed to supporting documentation.

4. Indexing/Cross-Indexing. No uniform indexing system is prescribed. However, indexes should be simple, expandable, and related to the audit plan to facilitate easy reference. Exhibit D (A:AM07EXD.WPF) illustrates an acceptable system of indexing.

a. When workpaper summaries or lead schedules are used as support, the information used must be cross-indexed and traced to source. Workpaper summaries or lead schedules are not considered complete until cross-indexes are entered on the workpaper.

b. Indexes and cross-indexes should be noted on workpapers as soon as possible. This practice facilitates the writing and summarizing process in that auditors can more easily note the source or location of relevant material.

c. Normally, the auditor who prepares a workpaper will also cross-index it to any supporting documentation. AICs and Audit Directors are to ensure that those workpapers prepared by staff assistants have been properly indexed and cross-indexed.

d. In preparing, indexing, and cross-indexing workpapers, auditors should try to anticipate how the information on the workpaper will be used to support a draft report. Where appropriate, the auditor should add notes or observations to the workpaper to show the significance of the information being presented and to allow reviewers to confirm the accuracy of any conclusions made. For example, an auditor might wish to make a statement in a draft report citing the range of 3 to 70 based on a 10-page workpaper schedule consisting of one or more columns of 300 numbers, with one column ranging from a low of 3 to a high of 70. To do so, the auditor should note on the workpaper what the range is and the pages on which the "high" and the "low" can be found. This statement can then be cited for support rather than referring to the entire 10-page schedule to support the range.

e. All cross-indexes cited will normally be to a specific page of a supporting workpaper--e.g., A1, p. 1. If a statement is cross-indexed to more than one supporting workpaper or to more than one page in a workpaper, the specific pages should be identified--i.e., A1, pp.1 & 6, not A1-A6.

f. In general, all facts shown in a workpaper--e.g., figures, amounts, dates and titles--must show a source, be cross-indexed to identical support in other workpapers, or have an adequate explanation of how the auditor determined a particular fact. A reviewer should not have to perform computations or obtain oral explanations to determine the source and validity of stated facts.

g. Where multiple items of information are needed to support a particular finding or conclusion, the auditor should normally prepare a work-

paper summary to tie together the evidence relating to a particular topic. However, the summary must be cross-indexed to the supporting workpapers, factual items traced to source, and computations verified.

5. Documentation of Supervisory Review. In accordance with audit standards for supervision and workpaper preparation, AIGA supervisors are to document their reviews of workpapers, as follows:

a. AICs are to initial and date the bottom of each workpaper prepared by staff assistants. They are also to prepare a memorandum for the record when Audit Directors, ARMs, or Regional Managers hold a job review that results in significant revisions to the approved audit program. This memorandum should be provided to the respective supervisors for their concurrence and then retained in the workpapers.

b. Audit Directors or ARMs are responsible for reviewing all workpapers prepared by AICs and selectively reviewing workpapers prepared by staff assistants. They should document their review by initialing and dating the bottom of workpapers reviewed or by recording their comments on review sheets.

(1) Any significant review comments should be recorded on review sheets and retained in the workpapers. These comments should be periodically reviewed to ensure that any problem areas with the audit are resolved prior to its completion.

(2) Differences of opinion between an auditor and a supervisor concerning accounting and auditing issues will be documented and presented to higher-level supervisors to be resolved.

c. Referencers will ensure that supervisory review has been adequately documented in accordance with the procedures provided in chapter 12, section E. However, they should particularly note the following:

(1) Referencers will note any significant workpapers that do not appear to have been reviewed by the AICs, Audit Directors, or ARMs. The notes are not to be cleared until the required review has been performed and documented.

(2) Audit Directors and/or ARMs are to review the referencer's notes and the disposition of such notes by the AIC. They may document this review by either initialing and dating the bottom of the referencing sheets or by preparing a memorandum recording the time, nature, and results of their review.

d. Regional Managers should periodically review the workpapers from selected jobs to ensure that the required supervisory review by Audit Directors and ARMs is being performed and documented and that problem areas are resolved prior to completion of the audit.

D. WORKPAPER ARRANGEMENT

Workpapers should generally be segregated into two broad categories: Current File and Permanent File. Workpapers germane only to the current

audit will make up the Current File. Workpapers that may be useful in planning and doing future audits will be retained in a Permanent File.

1. Current Files. The material in the current files should consist of information relating primarily to the current assignment and not considered of continuing use for succeeding assignments.

- o Tables of contents and administrative material pertaining to the current assignment (e.g., audit profile sheets, survey program, end of survey decision contract, and detailed audit program);
- o Indexed and referenced copy of official draft report, referencing comments, tentative findings, management comments, and related material;
- o Schedules, summaries, and other workpapers arranged according to the table of contents;
- o Memoranda of interviews, telephone conversations, etc.; and
- o Any other material not considered of sufficient interest to retain in permanent files, but which is necessary to support the findings and conclusions reported for the current assignment.

2. Permanent Files. Permanent files contain information of a continuing or recurring nature which may be used in succeeding assignments. These files serve as a data base to assist in planning future work, as well as readily accessible summary information on work already performed and on reports issued.

a. Permanent files will generally include reference material pertinent to an auditee or activity under review such as:

- o Summary information on work already performed and on reports issued, including a listing of major areas covered in prior assignments, the approximate dates the work was done, and the result of such work;
- o A record showing disposition of current files no longer retained at the audit site;
- o Historical or background data (legislation, GAO audit coverage, budget information, and statistical data);
- o Description of the organization, personnel, functions, responsibilities and mission of the auditee or activity; and
- o Descriptions of management policies and controls, including internal review methods.

b. Regional Managers are responsible for establishing procedures within a region for the segregation, periodic review, and retention of permanent workpaper files. Material that is obsolete or no longer pertinent should be removed from the files and disposed of in an appropriate manner.

E. WORKPAPER RETENTION AND SAFEGUARDS

Auditors shall use reasonable care in safeguarding workpapers. Normally, workpapers and report drafts should be placed in a desk or file cabinet at the end of a workday. Special safeguards should be used for storing and safeguarding classified information, Privacy Act information, and other particularly sensitive material, such as proprietary data, plans for future operations (such as planned procurement actions), and information obtained to support fraud investigations or special congressional requests. Automated workpapers require special precautions to limit access, protect them from accidental destruction or alteration, and to otherwise ensure their physical protection and usability.

1. Workpaper Retention. Workpapers must be retained and disposed of in accordance with an approved Records Inventory and Disposition Schedule.

a. Permanent files may be retained by the Regional Offices as long as the information is considered of value in planning or conducting future audits.

b. Current files should be kept by the Regional Offices for at least 2 years after an audit report is completed or as long as unresolved issues remain regarding open audit recommendations. All other files should be transferred to an appropriate local Records Holding Area or Federal Records Center for storage, with destruction of the records 8 years after the fiscal year in which an audit was completed.

2. Physical Protection. Workpapers will be protected to make sure they are only accessible to authorized persons. Also, workpapers will be considered DOE property and will not be removed from the audited activity without supervisory approval.

a. During the day, auditors should not leave workpapers in places accessible to the public, personnel of the audited activity, or other unauthorized persons.

b. Unclassified working papers generally do not require special handling and auditors may store them in unlocked containers within DOE offices.

3. Special Precautions Required for Certain Material. Workpaper files which contain classified or sensitive information will be subject to the same retention policies as those pertaining to unclassified files. However, the storage, handling and disposal requirements for these files will vary.

a. Classified Information - Detailed instructions regarding the handling, controlling, storing and mailing of classified information are contained in DOE Order 5635.1A, "Control of Classified Documents and Information," issued 2-12-88, and in OIG Directive IG-908B, "Classified Document Control," issued 2-11-93. All OA personnel, including staff auditors and auditors under contract, must be familiar with and observe the procedures and controls established by these instructions for safeguarding all classified information that comes into their possession. For classified computer processing, OIG personnel will adhere to requirements of the classified

computer security program at the host site, including all technical provision of that program.

b. Sensitive Unclassified Information - Sensitive unclassified information will be protected against accidental disclosure and arousing curiosity. Laws and regulations which govern the dissemination of certain sensitive unclassified information will be strictly followed. Sensitive unclassified information will be identified and protected in accordance with guidelines established in OIG Directive IG-913, "Identifying and Protecting Sensitive Unclassified Information", issued March 31, 1993. Examples of sensitive unclassified information include:

- o Official Use Only. Official Use Only information must be handled in such manner as not to arouse the curiosity of people who do not have a need to know the information. Official Use Only information shall be stored in a reasonable and adequate manner when unattended, such as in a desk drawer or file cabinet.
- o Limited Official Use Only. Limited Official Use Only is a Department of State marking for privileged information. It covers material which may include, among other things, information received from privileged sources and certain personnel, investigative, medical, commercial, and financial records. Such material within the OIG shall be handled and stored in the same manner as DOE Confidential.
- o Unclassified Controlled Nuclear Information (UCNI). UCNI is unclassified information whose unauthorized dissemination is prohibited under Section 148 of the Atomic Energy Act of 1954, as amended. See Doe Order 5635.4, "Protection of Unclassified Controlled Nuclear Information", issued 2-3-88; and DOE Order 5650.3A, "Identification of Unclassified Controlled Nuclear Information", issued 6-8-92 for UCNI protection requirements.
- o For Official Use Only. For Official Use Only is a Department of Defense term and equates to DOE's Official Use Only. For Official Use Only is treated in the same manner as DOE Official Use Only.
- o Other. Other sensitive unclassified information may include personnel, medical, contractual, and financial data. Laws and regulations regarding dissemination of this information may carry criminal and civil penalties if ignored. Examples of other sensitive unclassified information include:

— Privacy Act - In compliance with the Privacy Act, the AIGA shall, among other things, (1) obtain only such information about individuals as is relevant and necessary, and (2) establish appropriate administrative, technical, and physical safeguards to assure the security and confidentiality of records and to protect against any anticipated threats and hazards to the security or integrity of these records. For example, any Privacy Act data obtained during an audit will be kept in locked cabinets and will be marked as follows:

WARNING: THIS WORKPAPER MAY CONTAIN PRIVACY ACT INFORMATION
(Do not release or discuss outside proper channels)

- Other Sensitive Information - includes information containing proprietary data, information involving sensitive personnel matters, data relating to possible civil or criminal law violations, congressional request material, procurement actions, plans for future DOE operations, and other unclassified sensitive information. Also, certain information may be prohibited from general disclosure because of Federal, State or local laws and regulations. All workpapers containing proprietary or sensitive information as described above should always be adequately controlled and safeguarded. Access to such workpapers should be restricted to authorized personnel with a need to have access to the information. Detailed instructions regarding the handling, controlling, and storing of proprietary and sensitive information are contained in DOE Order 5635.4 and in OIG Directive 913.

For all unclassified computer processing, all OIG personal computers will be denoted as "Sensitive Unclassified" systems. All unclassified computer processing will be done in conformance with the OIG Master ADP Security Plan for Unclassified Sensitive Support Systems, dated March 23, 1992.

SAMPLE COVER SHEET FOR WORKPAPER BUNDLE

AUDIT WORKPAPERS

Agency/Office:

Title of Audit:

Audit Location(s):

Date(s):

IGDMS Project No.: _____

BUNDLE _____ OF _____

Brief Description of Bundle Contents:

WORKPAPER RETENTION (Check one)

() Current File

() Permanent File

TO BE DESTROYED ON OR AFTER _____

FORMAT FOR MEMORANDUM OF INTERVIEW

PARTICIPANTS: N. E. Auditee, (Person Interviewed)
Suzie Q. Newperson, Auditor, IG-34, 353-xxxx

DATE: _ :00 _ .m., _ day, _ , 1990

PURPOSE: Describe the purpose of interview in 2-3 lines, such as
"To discuss selected issues concerning _____
and to obtain Auditee's views on how his organization
deals with those issues."

DISCUSSION:

The following statements were made and questions asked during the course of the meeting.

1. Opening comments.

- a. Ms. Newperson opened the meeting by . . .
- b. N. E. Auditee made these opening remarks . . .
- c. N. E. Auditee then responded as follows to selected questions.

2. Question . . . ?

Response

3. Other observations or comments made during the meeting.

- a. The Auditor should normally prepare questions in advance. These questions can then serve as a structure for conducting the interview and a checklist to ensure that all questions were asked.
- b. In writing up "Memorandum of Interview," Auditor can add comments made by N. E. Auditee without having to retype questions.
- c. Do not hesitate to ask for copies of documentation to support comments that N. E. Auditee may have made.
- d. Where a followup meeting may be needed, it is often desirable to conclude the interview by indicating that Auditor may contact N. E. Auditee for further information as the audit progresses. Also, if several persons were in the meeting, ask who should be your primary point of contact (POC).

FORMAT FOR WORKPAPER SUMMARY

WORKPAPER TITLE: _____

PREPARED BY: _____

DATE PREPARED: _____

A. OBJECTIVES, SCOPE & METHODOLOGY

1. Objective (Purpose) - Clear statement of the purpose of the summary.
2. Scope of Work Performed - Describe the extent of work performed which serves as a basis for the findings.
 - a. Describe activities covered, time periods covered (e.g., records reviewed for fiscal year _____), etc.
 - b. Describe when work was performed, to include start and finish dates, and locations visited.
3. Methodology - Describe procedures used to obtain information (e.g., interviews, walk-throughs, transaction testing, etc.). If advanced audit techniques were used, such as statistical sampling or computer-assisted audit techniques, the procedures used should be described in detail.

B. BACKGROUND (If Needed)

[No set format is prescribed. However, this section could be used to provide general criteria or other background information.]

C. RESULTS OF WORK PERFORMED

[This section should lay out statements of fact based on the work performed and the source of any evidence obtained. It should not include conclusions drawn from the evidence.]

D. CONCLUSIONS

[This section should provide an analytical summary of the facts as they pertain to the issue being discussed (includes a statement of the problem).]

E. RECOMMENDATIONS

[This section should describe what needs to be done to correct the problems noted.]

ILLUSTRATION: WORKPAPER INDEXING SYSTEM

CONTENTS -- _____ (Audit Title) _____

- A ADMINISTRATIVE (See detailed examples)
- B BACKGROUND
 - BA Background Summaries & Related Material
 - BB General Background
 - BC GAO Reports on _____ & Related Subjects
 - BD OIG Reports on _____ & Related Subjects
 - BE Other DOE Reports
 - BF Other Federal (Non-DOE) Reports
 - BG Newspaper/Magazine Articles
 - BH Other General Background Information (if needed)
- C CRITERIA
 - CA Administrative, Summaries & Related Material
 - CB Statutory (Public Laws, U.S. Codes, Etc.)
 - CC Federal Regulations/OMB Circulars
 - CD DOE Orders
 - CE Standards and Guidelines
 - CF Other Criteria or Related Material
- D SURVEY ANALYSES
 - DA Draft survey results
 - DB Summary spreadsheets
 - DC Site summaries
 - Etc. Open; Use as needed
- E SUBORDINATE ACTIVITY No. 1 (See detailed examples)
- F FIELD ACTIVITY No. 1 (See detailed examples)
- G COORDINATION WITH OTHER AGENCIES (See detailed examples)
- H Open; use as needed.
- thru
- Z

DETAILED LISTINGS

- A ADMINISTRATIVE BUNDLE
 - AA Open; Use as needed
 - AA-1 Open; Use as Needed
 - AA-2 Job File for Code __/__/__.
 - AA-3 End of Survey Decision Contract, __/__/__.

AB Report Processing

- AB-1 Open; Use as Needed.
- AB-2/1 Reserved for Final Report & Agency Comments.
- AB-3/1 Reserved for Official Draft & Agency Comments.
- AB-4/1 Reserved for TF&R(s) & Agency Comments.
- AB-5/1 Draft Outline(s) of Proposed Report

AC Job Authorizations/IGDBMS Reporting

- AC-1 Open; Use as Needed.
- AC-2 Notification Letter, __/__/__.
- AC-3/1 Memo of Formal Entrance Conference with _____, __/__/__.
- AC-3/2 Memo of Entrance Conference w/ (subord. activity), __/__/__.
- AC-3/3 Memo to File re. _____ Waiving Entrance Conf., __/__/__.
- AC-4/1 Memo re. Points of Contact
- AC-5/1 Audit Profile(s)

AD Audit Programs/Objectives

- AD-1 Open; Use as needed
- AD-2 Audit Objectives, __/__/__.
- AD-3 Survey Program, __/__/__.
- AD-4 Review Program/Detailed Verification Steps, __/__/__.

B Detail omitted from this example
thru
D

E SUBORDINATE ACTIVITY NO. 1 (SA)

- EA Open; Use as Needed
- EB-2/1 Memo of Activity Entrance Conference, __/__/__.
- EB-2/2 Memo of Meeting w/ _____, SA-1, __/__/__.
- EB-2/3 Memo of Meeting w/ _____, SA-2, __/__/__.

F FIELD ACTIVITY NO. 1 (FA)

FA Open; Use as Needed

FB-2/1 Memo of Field Activity Entrance Conference, __/__/__.

FB-2/2 Memo of Meeting w/ _____, FA-1, __/__/__.

FB-2/3 Memo of Meeting w/ _____, FA-2, __/__/__.

G COORDINATION WITH OTHER AGENCIES

GA Open; Use as Needed

GB U.S. General Accounting Office (GAO)

GB-1 Open; Use as Needed

GB-2 Record of meeting w/ GAO officials, GAO, __/__/__.

GC Dept. of Defense (DoD)

GC-1 Open; Use as Needed

GC-2 Memo of Meeting w/ _____, DoD, __/__/__.

GD State of _____

Etc.

H Detail omitted from this example
thru
Z

CHAPTER 8ADVANCED AUDIT TECHNIQUESA. SCOPE OF CHAPTER

This chapter sets forth policies and procedures to be followed in using computers, ensuring that data obtained from computer-based systems is reliable and accurate, and utilizing computer-assisted or other advanced audit techniques.

B. AUDITING IN A COMPUTER AGE

To prepare objective and convincing audit reports, it is necessary for auditors to obtain sufficient and relevant information and to analyze it in accordance with generally accepted government auditing standards. In today's computer age, this requires auditors to be able to (1) audit organizations where ADP or computer operations are an integral part of the operations being evaluated, and (2) use computer-assisted or other advanced audit techniques to collect and analyze audit evidence. This auditing environment requires that the audit staff collectively possess adequate professional proficiency to conduct audits in accordance with applicable audit standards. In addition, the extent of DOE activities in relation to limited OA staff requires that auditors make the best possible use of available resources. Even if not required, using computers or other advanced audit techniques can often be the most economical and effective way to accomplish audits.

1. Day-to-Day Use of Computers. The AIGA encourages the use of uniform computer procedures by auditors and support staff in daily operations, to include data collection and analysis, report processing and transmittal, and communications. To facilitate this, computer hardware and software is to be standardized throughout headquarters and field units.

a. Computer Hardware - Within OA, the IBM PC and IBM PC compatible are to be used as the basic desktop and portable computer work stations. The portable units are to be shared, as needed, to meet work requirements where portable computers are needed. The acquisition of computer hardware not in keeping with this standardization goal is discouraged. All hardware acquisition should be coordinated with AIGP's Office of ADP.

b. Computer Software - The AIGA will approve a standard software package for word processing, spreadsheet, data base, communications, and file to file transfers.

(1) Word Processing. All reports are to be prepared using the standard word processing software. The use of word processing software other than the selected standard is not approved or justified.

(2) Spreadsheets and Database Files. Auditors are encouraged to use the standard spreadsheet and database software in their data collection and analysis. The use of compatible software is permissible.

(3) Electronic Mail and Data Communications. The standard communications software is to be used for all E-Mail, file to file transfers, use of IGDBMS, or other communications requirements.

c. Quality Control Responsibilities - Auditors should use special care to ensure that information generated by use of personal computers, such as by using spreadsheet or database functions, is reliable, current, and consistent with its intended use. In general, auditors should comply with the following procedures:

- o A copy of computer-data files generated should be retained on diskette in the workpaper files for use in follow-up audit efforts or if questions are raised as to the validity of the information in the files.
- o The workpapers should contain a print-out of data in a computer-data file and cell definitions (especially formulas). Where appropriate, the information should also be cross-indexed to source documentation and traced to source.
- o The workpapers should contain a memorandum that explains steps taken by the audit staff to assure reliable and accurate processing of data.

2. Developing Advanced Technical Capabilities. AP³ is responsible for developing an internal capability to (1) undertake reviews of ADP systems that support agency missions and programs in its area of responsibility and (2) assisting regional offices in utilizing computer-assisted or other advanced audit techniques.

a. The requirement for an internal capability can be satisfied either by ensuring that regional staff have the necessary training and skills or by obtaining assistance from the AP³ ADP and Technical Support Division.

b. In general, audit work involving ADP and other advanced audit techniques should be coordinated in advance with the Director, ADP and Technical Support Division within AP³, and with the DAIG/AO. The ADP and Technical Support Division can assist the audit team in areas requiring technical expertise, and AO can address broader management functions. For example, they can help to ensure that the audit team is aware of

- o any prior AIGA, GAO, or other audit coverage involving general and application controls or tests of data reliability that may satisfy audit objectives;
- o known vulnerabilities, weaknesses or risks involving common systems software or major applications such as the Department's Integrated Payroll/Personnel System (PAY/PERS) or Procurement and Assistance Data System (PADS);
- o appropriate criteria for reviewing general and application controls, such as relevant DOE orders or Federal Information Resources Management Publications (FIPS PUBs);

- o known Departmental procedures, such as internal reviews that may address the adequacy of general or application controls; and
- o required knowledge, skills or abilities needed in order to adequately review an auditee's general or application computer controls, test data reliability, or to effectively use computer assisted audit techniques.

3. Obtaining Data Already On a Computer. If an auditee maintains and processes necessary audit information on a computer, the most effective and efficient way to obtain the data may be to either obtain a copy of the data base or to obtain on-line access to the data. The considerations for using such data are the same as for that obtained from other sources--it must be consistent, valid, and reliable. Accessing an existing data base can have tremendous advantages in that it may allow testing of an entire universe rather than restricting audit analysis to a limited sample.

a. Accessing Existing Data - Several options exist for the auditor. He or she can either obtain on-line access to the data base, obtain a copy of an existing data base, or arrange for the auditee to provide extracts of the necessary information. Each of these approaches has its advantages and disadvantages.

(1) In order to obtain on-line access to a data base, auditors will normally have to obtain permission from the custodian of the data, as well as the necessary account numbers, passwords, etc. In addition, auditors need to ensure that they have the necessary ADP skills to make efficient and correct use of this access. They should also request "read-only" access to ensure that they do not inadvertently change or destroy existing data, nor will management have a basis for accusing them of having done so.

(2) Normally, it is more efficient to obtain data in a computer-readable format, such as on tape or diskette, rather than converting the data to paper documents. However, if auditors are offered a copy of a data base, such as on a mainframe tape, they need to ensure that they have access to hardware which is compatible with the form in which the data is received, can make efficient and effective use of the data, and can store the data in accordance with workpaper retention guidelines.

(3) In many cases, it may be more efficient for the auditee to extract the necessary data from the computer-based system and to provide it in hardcopy form to the auditor. The auditor, however, needs to ensure that the data provided is a reliable and correct representation of the data in the system.

b. Security Considerations - Each staff member who has access to a controlled computer system is responsible for complying with the provisions of OIG Directive IG-110A, "Protection of Users Identifiers (I.D.s) for Access to Computer Systems," issued 2-8-90. In accordance with this Directive, staff members and contract employees will not share user identifiers or passwords other than those designated as shared office accounts. Regional Managers and audit directors are responsible for ensuring that this Directive is enforced within their respective offices.

4. Ensuring Reliable Data from Computer-Based Systems. When information from computer-based systems is an important or integral part of an audit, the reliability of that data becomes crucial in achieving audit objectives. In such instances, auditors are responsible for either (1) reviewing general and application controls or (2) conducting other tests and procedures to ensure the reliability of the data being used. In addition to the guidance below, the GAO publication Assessing the Reliability of Computer-Processed Data should be consulted in designing a methodology for assessing data reliability. (See also the requirement in the sample survey program, A:AM06EXB.WPF).

a. Determining How to Assess Reliability of Data - Normally, the AIC will be the most knowledgeable person on an assignment. As such, he or she is responsible for determining if data from computer-based systems is critical to the audit results. If the data is considered critical, then the audit team is responsible for coordinating with supervisors within their region (i.e., with their Audit Director or ARM) and with AP³ and AO to obtain concurrence on the level of review and testing needed to ensure the reliability of computer-processed data to be used during the audit. However, if the information is not critical to the audit results, then citing the data source will usually satisfy the accuracy and completeness reporting standards.

b. Reviewing General and Application Controls - When computer operations or computer generated data are an important integral part of the operations being audited, the audit work should include an appropriate examination of the general and application controls in the computer-based systems, including such tests as warranted. In reviewing the controls, the auditors are to consider the effectiveness of those general controls relevant to the specific application being reviewed, as well as those controls that are unique to the application being reviewed. These types of reviews, however, are major undertakings and should be coordinated through AO and AP³.

(1) General Controls. General controls include the plan of organization and methods and procedures that apply to the overall computer operations in an auditee's computer center. Reviews of general controls should generally address such areas as (1) organization and management controls, (2) security controls, and (3) systems software and hardware controls. Reviews of general controls should seek to determine whether

- o the controls have been designed according to management direction; and
- o the controls are operating effectively to provide reliability of, and security over, the data being processed.

In general, AP³ is responsible for assisting auditors in establishing an audit program for auditing general controls in major computer centers, in ensuring that the audit staff has the necessary technical skills, and in determining the frequency of such audits.

(2) Application Controls. Application controls are designed to ensure the authority of data origination, accuracy of data input, integrity of processing, and verification and distribution of output. Specific controls that should be addressed include those for

- o ensuring that only authorized data is input, and that it is processed promptly, accurately, and completely;
- o protecting the integrity of the application software, to include ensuring that the software and later modifications are authorized and tested before implementation; and
- o ensuring the integrity of output, whether in a batch mode or on-line, and the correct and timely distribution of outputs produced.

In general, AP³ is responsible for assisting auditors in establishing audit programs, ensuring that the audit staff has the necessary technical skills, and determining audit frequencies for auditing the Department's major computer applications, such as the

- o Central Personnel Clearance Index System (CPCI);
- o Departmental Integrated Standardized Core Accounting System (DISCAS);
- o Financial Information System (FIS);
- o Integrated Payroll/Personnel System (PAY/PERS);
- o Nuclear Materials Management and Safeguards System (NMMSS);
- o Procurement and Assistance Data System (PADS); and
- o Other systems identified by management or auditors as being particularly sensitive or critical to Departmental operations.

c. Testing for Data Reliability - If audits of general and application controls have been performed within recent years, auditors should cite them as a basis for relying on data from computer-based systems. However, if such controls have not been reviewed or have been found to be unreliable, the audit staff should perform specific tests to assure that the information that they desire to use is reliable, current, and consistent with its intended use. Such testing could include:

- o Processing test transactions through the system;
- o Tracing selected information in the system to source documents or performing physical counts or inspections;
- o Confirming the accuracy and integrity of data in the system by interviewing sources independent of the auditee--i.e., third parties such as regular users or suppliers of data from the application; and
- o Reviewing the auditee's own test procedures and results and determining any limitations on how the information can be used or control weaknesses.

The results of such testing should be documented in the workpapers, such as by preparing a flow chart that identifies system controls over the data, and cross-indexed to the computer data, audit program, and final report. If such testing is not performed, the auditors should ensure that their audit program is adjusted to reflect any necessary changes in audit objectives, scope and methodology.

5. Using "Computer Matching" Techniques. Auditors may determine that it is desirable to use "computer matching" techniques to compare data in one information system with that in another. This technique involves the comparison of two or more automated files to obtain a list of data elements that meet specific criteria. For example, this could include listing persons who, potentially, have violated program rules or regulations, or to otherwise identify irregularities that may indicate fraud, abuse or error. However, auditors need to be aware that DOE policy prohibits computer matching until the Head of a Departmental Element has assessed the costs and benefits of a proposed computer matching application, and the assessment has been reviewed and approved by DOE Headquarter's Privacy Officer.

6. Reimbursement for ADP Services. In carrying out audit responsibilities, auditors should not hesitate to obtain information from computer-based systems or to accept assistance from the auditee in obtaining such information. However, it is not OA policy to reimburse auditees for their costs when such assistance is provided. OA's position is that an audit is an integral part of an organization's management control system and, as such, the ADP resources required by auditors represent appropriate costs to the organization being audited.

C. STANDARDIZED DATA COLLECTION TECHNIQUES

On some audits, it is necessary to collect data from multiple sources in a standardized format in order for audit objectives to be achieved. However, such data collection can be costly, time consuming, and subject to certain constraints, even if conducted as part of a sampling plan (See section D of this chapter). Auditors should ensure that they are not requesting information that can be readily obtained from literature searches, agency files, contractor reports or unstructured interviews, and that they minimize the burden on respondents asked to furnish information.

1. Types of Data Collection Instruments. The major types of data collection instruments are "pro forma" workpapers, structured interviews, telephone interviews, and mail questionnaires.

a. "Pro forma" workpapers are generally used when reviewing and recording information in a standardized format from an auditee's files or from records maintained by persons or organizations affected by a DOE program.

b. Structured interviews involve the scheduling of face-to-face interviews in order to fill out a standardized questionnaire. Because this approach can be costly and time consuming, auditors need to be sure they have justified such methodology before it is adopted.

c. Telephone interviews are a special form of a structured interview. Although they are relatively quick and inexpensive, auditors need to ensure that they can justify the time required of respondents.

d. Mail questionnaires are considered the least expensive method for collecting information on a wide scale. However, considerable time can be expended in preparing and testing questionnaires and in followup to ensure an adequate response rate.

2. Approval Procedures. In some cases, data collection instruments could be subject to Departmental or OMB approval procedures. For example, DOE Order 1322.2C, "Forms Management," 10-22-91, states that "information collections" must be approved by OMB. This Order defines an "information collection form" as a written report, application, schedule, or other similar vehicle calling for the collection of information from the public. More importantly, under this Order, M&O facility contractors, offsite contractors, and financial assistance recipients are considered to be the public. Therefore, the following procedures will be followed for standardized data collection instruments:

a. Questionnaires or structured interview forms must be submitted to and approved by the DAIG/AP³ prior to their use if they will involve ten or more private citizens (e.g., participants in DOE programs), private firms, or local governments; five or more State governments; and twenty-five or more officials or employees of DOE or other Federal agencies. The DAIG/AP³, will be responsible for determining the coordination, if any, required within the OIG or with the Department's designated official for forms management.

b. Data collection instruments that will be used one time and are not considered to be information collection or interagency forms do not require approval or form numbers. However, Regional Managers shall ensure that there is a legitimate need for the form before it is used.

3. Planning and Pretesting an Approach. Effective use of questionnaires or structured interview forms requires that the instruments be pretested. Auditors have to determine which type of collection instrument to use and to ensure that the questions to be asked will elicit the appropriate response.

4. Data Collection and Analysis. After the information is received back from respondents, it has to be tabulated and analyzed in terms of the audit objective. Auditors need to determine in advance how they will transfer information from questionnaires to spreadsheets or other data base, the response rates required for valid data, and how to deal with invalid responses.

D. SAMPLING TECHNIQUES

Sampling is a process of examining or measuring a smaller group of items, called a "sample," in order to draw conclusions and make generalizations about a larger group of items, called a "universe" or "population." In order to make valid conclusions and generalizations about a universe, the

sample must be selected from and must be "statistically" representative of that universe. In some cases, nonstatistical samples may be of value in our work, but they must be used with care to avoid drawing invalid conclusions.

1. Statistical Sampling. Audits based on statistical sampling must be designed to ensure that the results are objective, defensible, and replicable. Since samples are based on the theory of probability, any charge that auditors looked only at the worst cases should have no standing. In terms of planning and managing audits that involve sampling, auditors should pay particular attention to the following characteristics or requirements:

a. Sample Size - In order to determine how large a sample is needed, auditors first have to determine answers as to the level of precision and the level of confidence needed. These answers, in turn, are dependent on the size of the universe, the types of analysis planned, and the type of sampling used. In general, the required sample size (n) is equal to the square of the factor for the desired confidence level (t) times the standard deviation (s) divided by the desired level of precision (E). In other words,

$$n = \left[\frac{ts}{E} \right]^2$$

b. Sample Frame - The sampling frame is a list of items contained in the universe. It should permit the sampler to identify and locate all items drawn into the sample and to differentiate this item from all other items in the sampling frame. For example, if the universe has been defined as the civilian work force at a contractor facility, the list of workers from which the sample is drawn should include all civilian workers as of a specific date, should contain no duplicate entries, and should contain no entries not in the universe.

c. Types of Samples - The major types of samples are simple (or unrestricted), stratified, and cluster samples.

- o Simple random sampling assumes that the population is homogeneous, is in one location, or can be sampled from a single frame if in several locations and that there is only moderate variation among the values of the items in the universe.
- o Stratified sampling occurs when the universe is divided into two or more parts and a random sample is selected from each part. This type of sample might be chosen if the universe is divided up among several locations and it is not possible to develop a single sampling frame.
- o Cluster sampling is the selection of groups of items rather than individual items. For example, the universe may consist of contracts, but the sample will consist of all contracts handled by selected contract offices.

d. Selecting an Unbiased Sample - In order that a sample may be used to make inferences about the universe, it must be based on the laws of probability. The basic methods of selecting statistical samples are random number sampling, systematic selection with a random start, and selection based

on randomly selected combinations of digits in lower order position (also called junior digit sampling).

- o Random number sampling is accomplished by using tables of random digits or computer-generated random numbers.
- o Systematic selection with a random start is a technique in which the desired sample size is divided into the number of items in the population. Items are then selected at the specified intervals based on a random starting point. For example, if an auditor desired to select 200 contract files from a universe of 10,100 files, he or she would (1) divide 10,100 by 200 to determine an interval of 50.5, (2) round down to the nearest whole number to get a sampling interval of 50, (3) determine a random starting point between 1 and 50--e.g., 36, and (4) then select every 50th item--i.e., the 36th item, 86th item, 136th item, etc. The items selected in this manner would constitute the sample.
- o Sample selection based on random combinations of digits in lower order positions can be selected when items in a universe are serially numbered. For example, an auditor could decide to review all personnel files where the last digits of an employee's social security number ended in 78.

e. Presenting Sample Results - Auditors must use extreme care in analyzing and presenting sample data. Efforts to draw conclusions as to variables involved, relationships between variables, and accounting for variations (such as through regression analysis) require the services of sampling experts. They must also remember that the purpose for drawing a sample is to generalize about the universe from which it is drawn. For example, if auditors selected samples consisting of 100 contract files at each of three audit sites, they might desire to present the combined results of their work. This could lead to inaccurate conclusions if the universe at each of the sites differs, such as 1,000 at one site, 5,000 at another, and 10,000 at the third. Combined results would be correct only if the sample results were weighted to reflect the differing number of contract files at each site.

f. Documentation Requirements - If statistical sampling is used, auditors will ensure that the workpapers include (1) the basis for sample selection; (2) size of audit universe; (3) attributes of the sample (error rates, sample interval, confidence levels, etc.); (4) results of the sample; and (5) basis for projecting sample results.

2. Nonstatistical Sampling. Nonstatistical samples, such as judgment samples, can be useful in conducting audit work. They are most often used as a form of discovery sampling to increase our knowledge about certain portions of a universe. For example, auditors may deliberately select cases in a particular universe that represent the largest dollar amounts or the greatest potential for error. However, the sample results must be used with care and cannot be used to draw valid conclusions about an entire universe.

CHAPTER 9GENERAL REPORTING POLICIES**A. SCOPE OF CHAPTER**

This chapter sets forth the purpose of written audit reports and identifies required report characteristics.

B. GENERAL REPORTING POLICY

The policy of the AIGA is to prepare and release a report to the auditee and other interested parties for each audit undertaken and completed by or on behalf of OA. The purpose of the written report is to provide to the auditee and other interested parties the findings and recommendations for corrective action that resulted from the audit. In those instances where the audit does not result in reportable findings or recommendations, a written report is still required in order to notify the auditee that the audit has been completed. A written notification is also required (letter report) for all audits terminated prior to completion.

C. EDITORIAL STYLE

In addition to this Manual, all OA reports and correspondence will follow the guidance in OIG Directive IG-203B, "Office of Inspector General Editorial and Writing Style," issued 3-12-93. If specific guidance is not found in this directive, the U.S. Government Printing Office Style Manual shall be used to supplement the directive and this Manual. The following OA style preferences should be adhered to for all reports.

1. Writing Style. As reports are written, the auditor should keep in mind that people in varied positions, such as the Secretary, senior DOE managers, Congress, and other external agencies, read and use our reports. Because our audience is diverse, readers may not be familiar with the details of the audit; therefore, results must be explained carefully. In general, audit reports should be written in the deductive style. Paragraphs should contain topic sentences that narrow and predict the scope of information to follow. Detailed support should flow from the topic sentence.

The auditor should write sentences and paragraphs that are short, clear, and concise; and strive to use the active voice whenever possible. Writing in the active voice is stronger, clearer, and shorter. Passive voice tends to leave out important information. Audit reports should be written in plain English and should avoid overly formal bureaucratic writing that is difficult to read and understand. The auditor should choose words that can be understood by those not closely associated with the Department.

2. Acronyms. Acronyms may be used (but should not be overused) when referring to particular organizations, programs, functions or documents. An acronym must be clearly identified or explained and should be used only when it will be referred to again in the report. The full name or title should be written out the first time it is used, and the acronym should follow in pa-

rentheses. As a minimum, an acronym should be fully identified the first time it is used in the report.

3. Use of Names. If the audit is a review of a program or an administrative process, the names of firms normally shall not be cited directly in the report. Firm names may be used for audits of a specific contract or grant. Normally, the names of individuals shall not be used in audit reports.

4. Visual Aids. Visual aids can be effective devices in capturing readers' attention and convincing them that corrective action must be taken. Pictures, charts, graphs, and other visual aids may be used in audit reports if they enhance the effectiveness of the presentation. When visual aids are used, the text just before them must tell the reader what to look for. Graphics or photographs will not be printed in color in OIG reports, manuals, and correspondence. Any exceptions to this policy will be reviewed and approved, on a case-by-case basis, by the IG or the Associate IG.

5. Highlighting. In general, the use of highlighting (such as boldface print or underscoring) should be reasonable, consistent, and appropriate. Although such techniques may be used to call attention to certain key words or phrases, they should not be used as a standard practice.

D. AUTHENTICATION OF AUDIT REPORTS

Authentication of audit reports indicates that a delegated senior OA official has reviewed and approved the report. The authentication provides assurances that the report was prepared in accordance with applicable professional standards and satisfies existing audit policy.

1. Reports Prepared by OA Staff. Audit reports are authenticated by the handwritten title "Office of Inspector General" that should be written with a black felt tip pen. An official file copy of the authenticated report is to be kept in the project file and the signature of the person authenticating the report and the date authenticated should be placed on the file copy beneath the authentication. The official file copy of a Blue Cover report shall be returned to the Regional office for inclusion in the project file. All audit reports, except letter reports, should be authenticated. Letter reports are to be signed by the appropriate issuing official.

The following officials are authorized to authenticate and sign audit reports:

AUTHENTICATION OF AUDIT REPORTS

<u>Official</u>	<u>Authentication Authority</u>
AIGA	- Reports to be issued by the Office of Inspector General and any other report as designated by the AIGA.
DAIG/AO	- For reports as designated by the AIGA.
Regional Managers	- Reports which the AIGA has authorized Regional Managers to issue (see para. E)

2. Reports Prepared by Auditors Under Contract. Each contract, grant, preaward and financial (of integrated contractor) audit report prepared for the OA by auditors under commercial contract is authenticated by the preparer prior to submission to the AIGA for its acceptance. Audit reports are authenticated using the firm name rather than the words "Office of Inspector General." Acceptance of contract, grant, and preaward audit reports by the OIG is accomplished by printing under this authentication the words ACCEPTED BY: (in caps and underlined) with the handwritten title "Office of Inspector General" appearing immediately below the ACCEPTED BY: line. The person accepting the report on behalf of the OIG will place his or her signature and the date of acceptance on the official file copy of the report. The same officials authorized to authenticate reports prepared by OA are authorized to accept, on behalf of the OIG, reports prepared by auditors under contract. The report is not an official report until it has been authenticated and accepted. Authentication of financial audit reports of integrated contractors is accomplished through the Regional Manager's transmittal memorandum forwarding the report to the appropriate field office.

All other reports prepared by contractors are authenticated pursuant to paragraph one above, "Reports Prepared by AIGA Staff."

E. ISSUANCE OF AUDIT REPORTS

The authority to issue audit reports depends upon the type and status of the report, as well as the sensitivity of the matters discussed in the report.

1. Final Audit Reports

The responsibility for issuing final audit reports is decentralized to the maximum extent possible to allow reports to be issued and appropriate timely corrective action taken. (See also chapter 11.)

a. Inspector General. The IG shall issue or sign transmittal memoranda for all final reports directed to the Assistant Secretary level or higher. In addition, the IG issues Blue Cover draft reports and other reports referred for that purpose by the AIGA. The IG also reserves the authority to issue any report that he may specifically designate.

b. AIGA. The AIGA shall issue and sign transmittal memoranda for all draft report versions directed to the Assistant Secretary level and any other reports the AIGA may specifically designate. (Types of reports are explained in chapter 10.)

c. Regional Managers. Regional Managers shall issue or sign transmittal memoranda for Buff Cover and Letter reports directed to DOE officials at a level below an Assistant Secretary, and all contract, preaward, grant, and integrated contractor audit reports. As appropriate, Regional Managers may further delegate the authority to issue or sign transmittal memoranda for contract and grant audit reports. However, this authority should be handled carefully to assure a quality product.

2. Sensitive Audit Reports

Although broad issuance authority has been delegated, audit reports of a sensitive nature shall be cleared with the AIGA prior to issuance. It will be the AIGA's responsibility to clear appropriate matters with the IG. Sensitive reports include those that

- o contain an adverse opinion or examples of gross mismanagement;
- o have a broad or far-reaching impact; or
- o are of particular interest to Congress, the media, or high level Departmental Officials.

3. Draft Audit Reports

It is OA policy not to release draft reports to anyone except the auditee. However, if written requests for draft reports are received from external sources, such as GAO or congressional sources; than referenced reports may be released upon the approval of the AIGA or the DAIG/AO. If there is a request to release an unreferenced report, then the decision will be referred to the IG.

F. REPORTING STANDARDS

OA policy is to fully implement Yellow Book reporting standards for all audits. Reporting standards for both financial and performance audits are briefly discussed below. In addition, further guidance on their implementation is found throughout Parts III, IV, V, and VI of this Manual.

1. Form. In accordance with the Yellow Book, written audit reports will be prepared to communicate the results of each audit.
2. Timeliness. Reports are to be issued promptly so as to make the information available for timely use by management and legislative officials, and by other interested parties.
3. Report Presentation. Reports should be complete, accurate, objective, and convincing, and as clear and concise as the subject matter permits.

The auditor should keep in mind that the basic purpose of an report is to outline a corrective action program for the audited activity and to document the audit results for others to use.

4. Introduction. Each report should have an Introduction section that discusses the purpose and objective of the audit. Reports will include detailed audit objectives of work performed. Unattainable objectives on request assignments should be explained. All objectives identified in the End of Survey Decision Contract must be addressed.

5. Scope and Methodology. Each report should describe the depth and coverage of audit work performed, as well as techniques used for gathering and analyzing evidence. Specifically, the scope should explain what was audited, where it was audited (location), and when it was audited. The methodology should explain the actions and techniques used to gather and analyzed information. This information should be individually tailored to describe the work actually done and should relate to the objectives identified in the End of Survey Decision Contract. It should, as applicable:

- o Explain the relationship between the universe and what was audited;
- o Include when and where the audit work was performed, i.e., identify timeframes, organizations, and geographic locations at which audit work was conducted;
- o Explain how the audit work was performed, i.e., cite the kinds and sources of evidence used, techniques used to verify it, and techniques used to analyze it,
- o If statistical sampling is used, describe the sample design and state why it was chosen; and
- o For computer-processed data which is critical to the audit objectives, assure readers that the information relied on is credible and reliable. (Additional discussions on assessing the reliability of computer-processed data are found in chapters 6, 8, and 10.)

6. Statement on Auditing Standards. A statement on auditing standards used shall be included in the scope and methodology section in the audit reports for both financial and performance audits.

a. Financial Statement - The appropriate statement to be placed in the scope section of each financial audit report involving the certification of financial statements is as follows:

The audit was performed according to generally accepted Government auditing standards for financial audits and included tests of internal controls and compliance with laws and regulations to the extent necessary to provide reasonable assurance that the financial statements were free of material misstatement.

b. Performance and Financial Related - The appropriate statement in the scope section for all other audits is:

The audit was performed according to generally accepted Government auditing standards for performance (or financial) audits and included tests of internal controls and compliance with laws and regulations to the extent necessary to satisfy audit objectives.

c. Departures from Standards - Any departures from audit standards should be clearly stated. The known effect on the audit as result of not following the applicable standards should also be disclosed. For example, if the scope of the audit required but did not include consideration of the internal control structure, this, along with reasons for such departure from standards, should be disclosed in the report.

7. Compliance With Laws and Regulations. The Yellow Book standards require reporting on tests of compliance with laws and regulations.

a. Financial - For financial audits, this report should contain a statement of positive assurance on those items which were tested for compliance and negative assurance on those items not tested. It should include all material instances of noncompliance, and all instances or indications of illegal acts that could result in criminal prosecution. Further information on this subject is contained in the Yellow Book, (chapter 5, para. 5.).

b. Performance - For performance audits that include an assessment of compliance with laws and regulations to satisfy the audit objective, the report should include all significant instances of noncompliance.

c. Examples of Noncompliance and Illegal Acts - Statements to the effect that management has not complied with laws and regulations must be supported by specific examples. If instances of noncompliance have been identified, the audit report should identify the specific law or regulation not complied with. Illegal or potentially illegal acts that could result in criminal prosecution and that were found during or in connection with any audit shall be reported to the extent permitted under the circumstances. However, auditors need to ensure that they follow the policies and procedures established in section D of chapter 4 and section H of this chapter.

Most importantly, whenever indications of fraud or other illegal acts are disclosed during an audit, the matter should immediately be referred, through the appropriate supervisory channels, to the DAIG/AO, who will coordinate the referral of the matter including the "Memorandum of Referral" with the Office of Investigations, in accordance with OIG Directive IG-904A. Following consultation with the AIGI or the AIGI's field representative, audit work will be continued on those elements of the audit which do not involve indications of illegal acts. For any audit which has been referred to the AIGI as well as those audits initiated because of alleged illegal acts, the report shall not be issued in any form until a clearance is obtained from the AIGI representative and OIG legal counsel.

8. Report (or Statement) on Internal Controls. The Yellow Book standards require reporting on internal controls. Additional information on evaluations of internal controls and reporting of the results can be found in Yellow Book, chapters 4 (para. 23) and 5 (para. 17) and in standards issued by the AICPA.

a. Financial - For financial audits, reports should include as a minimum: (1) the scope of the auditor's work in obtaining an understanding of the internal control structure and in assessing the control risk; (2) the entity's significant internal controls or control structure including the controls established to ensure compliance with laws and regulations that materially affect the financial statements and results of the financial related audit; and (3) the reportable conditions, including the identification of material weaknesses, identified as a result of the auditor's work in understanding and assessing the control risk.

b. Performance - For performance audits that assessed internal controls to satisfy the audit objective, the reports should identify the significant internal controls that were assessed, the scope of assessment work, and any significant weaknesses found during the audit. For such audits, the "Scope" section of the audit report should contain a statement or paragraph similar to the following:

We assessed the significant internal controls with respect to (identify the significant controls assessed). Our assessment consisted of (describe the scope or extent of assessment). Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit.

9. Noteworthy Accomplishments. Reports should include a description of any significant noteworthy accomplishments, particularly when management improvements in one area may apply elsewhere. The inclusion of such accomplishments may also lead to improved performance by other Government organizations reading the report.

10. Issues Needing Further Study. If the scope of the audit or other factors limit the auditor's ability to inquire into certain matters that should be studied, the report should include a listing of any significant issues needing further study and consideration, and why further study is required.

11. Privileged and Confidential Information. Reports should state the nature of any information omitted because the information is prohibited from general disclosure and the requirement that makes the omission necessary.

12. Audit Findings and Conclusions. Reports should contain a full disclosure of the significant audit findings and, where applicable, the auditor's conclusions.

13. Cause and Recommendations. Reports should include the cause of the problems noted in the audit and recommendations for corrective actions when called for by the audit objective.

14. Views of Responsible Officials. Reports should include (1) the pertinent views of responsible officials of the organization, program, activity, or function audited concerning the auditor's findings, conclusions, and recommendations, and (2) what corrective action is planned.

15. Classified and Confidential Information. Auditors need to take precautionary actions when dealing with classified information, documents marked "Official Use Only," proprietary data, information involving sensitive personnel matters, data relating to possible civil or criminal law violations and information affecting the national security of the U.S. (see chapter 7 for details).

G. REPORTING REQUIREMENTS FOR ILLEGAL ACTS - ALL AUDITS

When illegal or potentially illegal acts are identified, the auditor is confronted with a special reporting problem. The Yellow Book requires reporting of all instances of illegal acts that could result in the audited entity, or an officer or employee of the audited entity, being subject to criminal prosecution. On the other hand, the Yellow Book also cautions that certain disclosures can interfere with legal processes, subject the implicated individuals to undue publicity, or subject the auditor to potential legal action.

While OA's reports will always be factually accurate as to audit findings, the details of matters referred to the AIGI for investigation should neither be discussed with parties outside the OIG, nor included in the audit report. The fact that a matter has been referred to the AIGI may be disclosed in the transmittal letter accompanying the audit report, upon approval of the AIGA and OIG legal counsel. The language to be included in the transmittal letter is prescribed and is highlighted on the next page.*

OA's policy is that the legal precept "presumption of innocence" is of paramount importance in deciding exactly what to disclose and how to disclose it. Faced with decisions regarding the obligation to disclose an instance or indicator of an illegal act in an audit report, OA will always give primary consideration to protecting an individual's presumption of innocence, and will extend that right to businesses. The table on page 9-8 should be used as a guide for handling disclosure of illegal acts and indicators or instances of such acts. For this purpose, indicators and instances are defined as matters having sufficient competent evidence to warrant their referral to the AIGI.

As indicated in the table, the current stage of the investigation or legal action must be considered. The stages are (1) preindictment, (2) postindictment, and (3) conviction or plea.

1. Preindictment. With respect to preindictment, care must be exercised in order not to compromise an investigation or to adversely affect an innocent person. To accomplish this result, the report transmittal letter may, upon approval, briefly mention the investigation by including the disclosure statement below. Details of the matters under investigation should be provided to the AIGI or his designee by separate confidential memorandum.

2. Postindictment and Conviction or Plea. With respect to post-indictment and conviction or plea, the report should contain appropriate details that are a matter of public record. Normally, a separate confidential memorandum is not required unless there are additional aspects of the audit requiring further review and analysis by the Office of Investigations.

3. OIG Legal Oversight. Any report with a transmittal disclosing instances or indicators of illegal acts (prior to indictment) shall be coordinated with IG legal counsel prior to release. This requirement applies to the first version, normally the TF&R, and any subsequent version in which the disclosure has been modified.

DISCLOSURE OF ILLEGAL ACTS
(OR INDICATORS OF SUCH ACTS)

	<u>Audit Situation</u>	<u>What MAY Be Disclosed</u>	<u>What MAY NOT Be Disclosed</u>	<u>Authority to Approve Disclosure</u>
VERBAL OR WRITTEN INQUIRY	Auditor receives an inquiry regarding a particular audit matter or contractor. (Includes inquiries from DOE procurement officials and similar officials from other agencies.)	Existence of an indictment, conviction, or plea.	Positive or negative confirmation of: allegations; OA referrals to the AIGI; existence of an investigation or fraud indicators resulting from audits or other sources.	Regional Manager or higher official in the OA chain of command.
PRE- INDICTMENT	Audit report to be issued covering a matter in which an OA referral to the AIGA has been made.	Existence of referral <u>may</u> be disclosed in the report transmittal letter.*	Details of referral.	Regional Manager, AIGA, AND OIG Legal Counsel.
POST- INDICTMENT	Audit report to be issued covering a matter in which there has been an indictment, conviction, or plea.	Details of indictment, conviction, or plea, as appropriate.		Regional Manager

* When disclosure of allegations, indicators, or instances of illegal acts is called for, OA's policy is to use the following language in the transmittal letter accompanying the report:

During the audit, certain matters came to our attention that were referred to the Office of Investigations (or other investigative organization to whom the matter was referred) for further review and analysis.

The above statement is not to be used unless a referral has actually been made.

CHAPTER 10TYPES OF REPORTS AND THEIR ORGANIZATIONA. SCOPE OF CHAPTER

This chapter defines the types and organization of audit reports.

B. TYPES OF REPORTS

The various types of reports issued by the AIGA and their purposes are identified below.

1. Blue Cover Report. Blue Cover reports are generally used to report audit findings of major significance to an appropriate Assistant Secretary or higher level. These reports are issued by the AIGA and the transmittal letter is signed by the IG. Reports containing recommendations to levels below the Assistant Secretary may also be issued as Blue Cover reports, if the subject matter and contents of the report are deemed of sufficient national interest, significance or sensitivity such that an Assistant Secretary or higher level should be informed.

2. Buff Cover Report. Buff Cover reports are generally used to report audit findings of major significance requiring action by management below the Assistant Secretary level. Regional Managers issue these reports and sign the transmittal letters.

3. Letter Report. Letter reports are generally used to close audits in which work has been completed and for which there were either no findings or findings with only minor significance. A Letter report may also be used to terminate an audit if for some reason the audit is terminated prior to completion. These reports are issued by the Regional Managers.

4. Financial and Financial Related Reports. OA issues a number of specialized financial or financial related reports. The major types are described below.

a. Financial Statement Report - The Chief Financial Officers Act of 1990 (CFO Act) requires financial statement audits for certain DOE components. Additional guidance on reporting the results of financial statement audits is provided on page 10-11.

b. Contract Report - Contract reports (excluding preaward audit reports) are used to report financial related audit activities of nonintegrated contractors. Examples of contract audit activities include, but are not limited to, direct and/or indirect cost incurred audits, defective pricing audits and accounting system reviews. These reports are issued and transmitted by Regional Managers to the office requesting the audit. See Part IV of this Manual for further guidance.

c. Preaward Report - Preaward reports are a type of contract audit (financial related) used to report the allowability of a prospective contractor's proposed cost. These reports are issued and transmitted by Regional Managers to the office requesting the audit. See Part IV of this Manual for further guidance on issuance of these reports.

d. Grant Report - Grant reports are used to report on grant recipients' financial operations and compliance with grant requirements of Federal grant programs, including those administered by DOE. Organizationwide audit reports of State and local governments are required by OMB Circular A-128 and are prepared by IPAs (CPAs and state auditors). These reports are issued to the grant recipients of Federal funds who in turn send the report to the Federal agencies supplying the funds. Within DOE, the reports are sent to the OIG regional audit office having assigned audit cognizance. In turn, the regional office performs the required reviews and assigns an audit report number before transmitting the reports to the responsible DOE contracting office for audit follow-up. Detailed information on DOE's A-128 responsibilities is found in Part V of this Manual.

e. VANEA Reports - Reports related to the signing of the Voucher Accounting for Net Expenditures Accrued (VANEA) are sometimes referred to as "VANEA audits." Although not an audit of the VANEA, the report entitled "Internal Controls That Assure Costs Claimed by and Reimbursed to the Contractor Are Allowable Under the Contract" provides certain assurances related to its signing. These advisory reports to the contracting officer are issued and transmitted to the field office by Regional Managers.

C. GENERAL REQUIREMENTS

To assist in producing uniform and professional quality reports, auditors should use standard report formats for the various types of reports. Standard formats can provide for a more effective and efficient means of reporting audit results to appropriate DOE officials and in obtaining the necessary corrective actions.

The nature of the audit (financial or performance) and the audit results will determine the specific report format to be used. The formats prescribed in this chapter will cover most reporting situations. Every effort should be made to conform to these formats. Major deviations from the prescribed formats can only be made with the approval of the DAIG/AO.

Financial audits and performance audits are two broad categories of audits recognized by GAO. The GAO definition of financial audits includes financial related audits. The Yellow Book states that financial related audits may come under the purview of either financial audits or performance audits, depending on the audit objectives. Contract, grant, and preaward audits are specific DOE audits that fall within the definition of financial related audits. The reporting requirements for financial audits are contained in the SASS issued by the AICPA and are supplemented by the Yellow Book. These issuances provide detailed instructions on the composition of financial audit reports and should be strictly adhered to. The reporting requirements of financial related audits categorized as contract, grant, and preaward audits are contained in Parts IV and V of this Manual. The requirements for VANEA audits are contained in chapter 22.

The reporting requirements contained in this chapter for Blue Cover, Buff Cover, and Letter reports are related to performance audits plus any financial related audits that fall into the performance audit category based on the audit objectives.

Interim versions of all types of reports or segments of the reports shall be in the same format as the final report except for obvious differences such as omission of report cover, report number, and date. These differences are identified in the discussion of each type of report. Preferably, final reports should use a "ragged" right margin.

D. BLUE AND BUFF COVER REPORTS

The formats for Blue and Buff Cover reports are the same, regardless of the number of findings. The following illustration shows the organization of these reports.

Blue and Buff Cover Report Format

- o Report Cover
- o Title Page
- o Table of Contents
- o Summary
- o Part I - Approach and Overview
 - Introduction
 - Scope and Methodology
 - Background
 - Observations and Conclusions
- o Part II - Finding(s) and Recommendations
- o Part III - Management and Auditor Comments
- o Part IV - Other Matters
- o Part V - Exhibits and/or Appendices

Each section of the Blue and Buff Cover report format is discussed below.

1. Report Cover. A standard report cover is used for all final Blue and Buff Cover reports. The Blue and Buff report cover should be prepared exactly as shown in exhibit A (A:AM10EXA.WPF). A report cover is used only on the final report; the title page is the cover on all interim versions.

2. Title Page. A standard title page is used for all Blue and Buff Cover reports. The title page should be prepared exactly as shown in exhibit B (A:AM10EXB.WPF). For draft reports, the phrase "OFFICIAL DRAFT" should be

stamped at the top of the title page, as well as subsequent pages, or included as a page header. The title of each audit report should begin with "Audit of...." Additionally, the report number and date are shown only on the final report.

3. Table of Contents. The Table of Contents should be prepared as shown in exhibit C (A:AM10EXC.WPF). It is a verbatim listing of the headings of the major sections and subsections of the report, with related page reference. The sections and subsections are listed in the same order as they appear in the report. The major parts of the Blue Cover report are identified with Roman numerals. Each finding included in the Findings and Recommendations section is identified with an Arabic numeral. Any appendices shall be identified with a capital letter.

4. Summary. The purpose of the Summary is to present a synopsis of the report to busy readers as quickly as possible. The Summary should (1) identify the activity or entity audited, (2) state the general purpose of the audit, (3) briefly describe the major finding(s), (4) include management reaction to the recommendations and their position on the facts and conclusion presented in the report, and (5) conclude with the authentication. It should generally not exceed one page. See exhibit D (A:AM10EXD.WPF) for an example.

The Summary should not contain a word for word recitation of the audit objectives, nor should it contain any information the busy reader is likely to find extraneous. This detail will be provided later.

5. Part I - Approach and Overview. Part I of Blue and Buff Cover reports consists of an introduction section that discusses the purpose and objectives, and sections on the scope and methodology, background, and observations and conclusions. An example of Part I is contained in exhibit E (A:AM10EXE.WPF).

a. Introduction - This section should include brief background information to indicate to the reader the significance of the subject matter of the audit. This section should also indicate to the reader the purpose and objectives of the audit. Generally, this section should be no more than one page.

b. Scope and Methodology - The scope of audit should be clearly stated in all reports and any limitations of scope should be explicitly identified. The areas or functions examined should be stated in nontechnical language so that the reader has a clear understanding of the audit coverage. Organizations and geographic locations at which audit work was conducted should be identified, as well as the time period covered in the audit. When necessary for clarification, the scope shall clearly identify areas not examined or specifically excluded from the audit.

This section should also describe the audit methodology used. It should explain the evidence gathering and analysis techniques used to accomplish the audit objectives and identify any assumptions made. If statistical sampling or other advanced audit techniques were used in the audit, their use should generally be explained. Appropriate details of the statistical sampling or other advanced audit techniques and their results should be included in Part II - Findings and Recommendations. Every effort should be

made to avoid any miscommunication concerning the work done to achieve the audit objective, particularly because of constraints on time and resources.

This section should also address the following additional requirements, as appropriate.

(1) Statement on Auditing Standards. The report shall state in this section that the audit was accomplished in accordance with generally accepted Government auditing standards. The precise language to be used is found on page 9-5. If one or more of the applicable standards were not followed, the report should disclose that fact, should give the reasons, and provide the known effect of not following the standard.

(2) Compliance with Laws and Regulations. This section should indicate the nature and extent of compliance testing.

(3) Internal Controls. This section should identify the significant internal controls assessed in accomplishing the audit objectives, should state the extent of the assessment including the control risk, and should include a reference to the report section which discusses any significant weaknesses found. The discussion of internal control weaknesses will vary depending on the significance of the weaknesses found and the relationship of those weaknesses to the audit objectives. Additional guidance for addressing internal controls is provided in chapter 9, pages 9-5 and 9-6.

(4) Data Reliability. For computer-processed data which is critical to the audit objectives, the Scope and Methodology section should assure readers that the information relied on is credible and reliable. Specifically, it should

- o Identify the scope of work done when system controls are relied on to reduce data testing;
- o Describe the testing of the computer-processed data, including the tests performed, their purpose, and the error rates disclosed; and
- o Present any factors known to limit the data's reliability and if significant, the sensitivity of the results to the accuracy of the data. (Additional information, including sample report language, is contained in the GAO publication Assessing the Reliability of Computer-Processed Data.)

(5) Exit Conference. This section shall state that an exit conference was either held or waived. It should show either the date the exit conference was held and the title of the highest management representative who attended or the title of the representative who waived the conference. Examples of appropriate language follow:

Exit Conference Held

An exit conference was held with the (title of highest management representative who attended such as Assistant Secretary, Defense Programs) on (date of conference).

Exit Conference Waived

An exit conference was waived by the (title of management representative who waived the conference such as Assistant Secretary, Defense Programs).

(5) Contractor Assistance. In cases where contractor assistance was used, the scope section should contain a statement to the effect that: "The firm of (name of contractor) participated with the Office of Inspector General in conducting this audit."

c. Background - Background information should be included as necessary to understand the issues presented in the report. This information sets the stage or provides the context by telling the reader about the entity being audited and the relevance of the area being audited. Background information may identify generally the criteria for the audit. Without this information, the reader would probably not understand the remainder of the report or its relevance. If the report does not require a Background section, it may be omitted.

d. Observations and Conclusions - This section summarizes the audit and tells what was found. No rigid format is prescribed so as to give the auditor maximum flexibility in writing. However, certain items must be covered in this section. Also, the auditor should put the report in perspective by identifying any constraints placed on management or the auditor, and any issues needing further study.

The auditor should respond to each audit objective. For balance, this section should include mention of what was being done right with respect to the objectives. It should also state what was wrong (the findings). Each finding in Part II must be identified. Major or significant recommendations in the report should become obvious to the reader of this section or should be addressed in general, but not verbatim, terms.

The prose used in summarizing the finding in this section will likely be shorter than that used in the opening paragraph of each finding in Part II. This section should include material instances (either individually or collectively) of noncompliance with laws, regulations and DOE orders, as well as material internal control weaknesses. For instructions on reporting illegal acts or potential illegal acts see chapter 9. In the allowability of certain cost is questioned, this fact should be discussed in this section with details provided in Part II. Exhibit E in chapter 14 (A:AM14EXE.WPF) provides suggested report language.

This section should not raise minor issues that are not discussed in Part II. Where appropriate, minor issues, including all minor noncompliance items, may be presented to management either verbally or in Part IV - Other Matters. The disposition of all minor items should be documented in the workpapers.

(1) Prior Audit Reports. This section may be used to provide general comments on actions taken on prior audit reports of the OIG, the GAO, or other organizations. If an in-depth discussion is considered necessary, additional details should be provided in an appendix to the report.

(2) Noteworthy Accomplishments. The observations and conclusions section may be used to provide a brief presentation of significant noteworthy accomplishments by management, especially where improvements made in one program or activity may be applied elsewhere. If a summary is considered appropriate for inclusion in this section, a more detailed discussion of noteworthy accomplishments should be presented in an appendix to the report.

(3) Issues Needing Further Study. If the scope of the audit or other factors limited the auditor's ability to address issues directly related to the audit objectives, they should be discussed here. If an in-depth discussion is considered necessary, additional details should be provided in an appendix to the report.

(4) Privileged and Confidential Information. Relevant information deemed privileged and confidential that was omitted from the report should be disclosed as follows:

Certain relevant information deemed privileged and confidential has been omitted from this report. This information will be provided on a need-to-know basis to those persons authorized to receive it.

(5) Internal Control Weaknesses. Weaknesses that should be noted in the auditee's yearend assurance memorandum should be mentioned here. Alternatively, the report may conclude that "Our limited review did not disclose any material internal control deficiencies."

(6) Budgetary Impact of Finding on the Deficit. If relevant, the observations and conclusions section should briefly summarize the monetary impact of the finding on deficit reduction.

6. Part II - Findings and Recommendations. This section should encompass the major findings resulting from the audit, including material internal control and compliance findings. It should not include findings of relatively little significance, because these findings tend to take away from the report's impact. If the findings do not warrant issuing a Blue or Buff Cover report but are significant enough to make a matter of record, they should be included in Part IV - Other Matters. Otherwise, minor findings are not mentioned in Blue and Buff Cover reports, but are communicated orally to responsible officials, normally at the exit conference.

Each finding shall begin on a new page and become a separate section within this Part. Each finding shall contain the following elements.

Finding and Recommendations

- o Caption
- o Finding (lead) Paragraph
- o Recommendation(s)
- o Management Reaction
- o Details of Finding

The elements of each section are discussed below. An example is shown in exhibit F (A:AM10EXF.WPF).

a. Caption - The caption of each audit finding should be objective, meaningful and stated in neutral terms. It should identify the audit subject and indicate the function, accounting area or activity concerned, such as "Case Processing" or "Accounting Procedures for Construction Funds." Inaccurate or incorrect captions may be misleading and indicate greater audit coverage or significance than actually presented in the report.

b. Finding Paragraph - The lead paragraph in each Findings and Recommendations section has two distinct functions: (1) it summarizes the entire finding; and, (2) it predicts the organization of the section. As a summary it must give enough information to stand alone; thus, it is a type of "pull out paragraph" containing the essence of the finding but not all the details. (Writers should remember, however, that a good technical summary should contain enough significant details to suggest the importance of the finding.) As an overview, the lead paragraph predicts the prescribed organization of the section. Once writers have set up this structure, they should not have major deviations. Thus, if writers define a situation as condition in the lead paragraph, they cannot discuss it as cause in the body of the section.

The lead paragraph should present as concisely as possible the overall situation covered by the "Details of Finding" section. It should state the (1) criteria; (2) condition found (problem or deficiency) in relation to the criteria; (3) causes of the condition or problem; and (4) resulting adverse effect of the condition. It should especially emphasize the management principle at issue, such as lack of internal controls, inadequate procedure, or unimplemented policy. The cause and effect also should be placed in perspective by establishing their magnitude in relation to the program, activity, or function audited. The recommendation should flow logically from the facts presented in this paragraph.

c. Recommendations - Recommendations shall follow the lead paragraph and should be specific in nature and addressed to the lowest DOE management level that can take corrective action. In some cases, the lowest management level will be an Assistant Secretary or even the Secretary. If recommendations are made to more than one official or manager, the officials or managers should be separately identified. The finding should be structured so that the recommendations relate to the cause of the adverse condition

AIM

Association for Information and Image Management

1100 Wayne Avenue, Suite 1100
Silver Spring, Maryland 20910
301/587-8202

Centimeter

Inches

MANUFACTURED TO AIM STANDARDS
BY APPLIED IMAGE, INC.

3 of 7

cited in the finding paragraph. Also, recommendations should be made to correct the current condition, such as adjusting the books or billings. The cause of the adverse condition must be substantiated through good audit techniques in order to develop a good recommendation. The recommendations should not address management weakness or adverse effect not identified in either the Finding Paragraph or the Details of Finding section.

Recommendations should be dynamic in nature and specify the type of management actions or changes needed to remedy the conditions noted. Vague recommendations, such as "a study or review should be made..." or "Management should coordinate with other activities to determine the feasibility of...", should be avoided since they may be used as an excuse for maintaining the status quo or delaying needed changes.

d. Management Reaction - This section should briefly describe management's reaction to both the finding and the recommendation (s). Greater detail on management's comments is provided in Part III.

e. Details of Finding - The details of finding should convince the reader that management should willingly take the desired corrective action. This section is an extension of the lead paragraph and should follow the sequence set up in the lead paragraph. Each attribute in the discussion should be clearly distinguished from the others, with the use of appropriate subheadings. The attributes and their normal sequence follow:

Details of Finding

- o Background (optional)
- o Criteria
- o Condition
- o Cause
- o Effect

Using these attributes will help auditors develop and organize their findings. Their use will also assist auditors in determining whether they obtained all pertinent information. Developing the attributes of a finding is discussed in greater detail in chapter 6.

It maybe appropriate in certain circumstances to discuss management's comments on the factual information presented in the details of the finding. Management's comments on the factual information may be included when it will provide better balance to the finding and ensure full disclosure all pertinent information.

7. Part III - Management and Auditor Comments. This section provides a synopsis of management's comments on matters discussed in the report and the auditor's assessment of the management comments on the report. Management comments germane to key points of each finding and recommendation should be summarized and followed immediately by the auditor's response. Comments

concerning the correction of facts or other matters with which the auditor agrees should be reflected by changing the report as appropriate and omitting or adjusting the comment as appropriate. If management indicates that prompt, positive, corrective action has been or will be taken, full recognition should be given. Conversely, if management's position is negative or does not concur with the finding and recommendation, a specific point-by-point rebuttal is necessary for the finding to remain viable. This may be done by providing additional information supporting the auditor's view or otherwise showing that management's comments were incorrect. If the auditor cannot adequately rebut management's lack of concurrence, the finding must be changed or deleted. The auditor's opinion of management's reply and attitude, (i.e., positive, nonresponsive, etc.,) may also be included in this section. An example of this part is shown in exhibit G (A:AM10EXG.WPF).

8. Part IV - Other Matters. This part of the report is optional and should be used to report minor findings that are not addressed in Part II, but are included in the report as a matter of record. This section, for example, may include immaterial instances of noncompliance and insignificant internal control weaknesses. In most circumstances, these matters should be communicated orally to the auditee at the exit conference, and the workpapers so documented. There is no established format for this section. However, the finding elements, to the extent they could be developed, should be presented in a logical sequence, except there should be no recommendations in this section. The usual rules of brevity, need, relevance, convincing, and clarity, should be considered. See exhibit H (A:AM10EXH.WPF) for an example.

9. Part V - Exhibits and Appendices. This section is optional and shall be used to display schedules or supplementary material necessary to support data contained in the body of the report. See exhibit I (A:AM10EXI.WPF) for an example.

E. LETTER REPORTS

Letter reports are used to close out audits that had no findings or only issues of minor significance. A letter report may also be used to terminate an audit if for some reason the audit must be terminated prior to completion. Letter reports are typed on DOE memorandum paper and signed rather than authenticated by the issuing official. See exhibit J (A:AM10EXJ.WPF) for an example of the format.

Initial paragraphs of a letter report should identify the audit's objectives, scope, and methodology, including statistical sampling and other advanced audit techniques used in accomplishing the objectives. Subsequent paragraphs should address what was found with respect to the objectives (normally positive accomplishments in a letter report) including the criteria, condition, cause, and effect related to any minor findings being reported. In some instances, we may wish to request management comments on our observations, but in no case should a letter report contain recommendations or require a Departmental position in accordance with DOE Order 2320.2B, "Establishment of Departmental Position on Inspector General Reports," issued 5-18-92.

The auditor should also adhere to the following standards for letter reports.

1. Yellow Book. The report shall state that the audit was accomplished in accordance with generally accepted Government auditing standards. If one or more of the applicable standards were not followed, the report should disclose that fact, give the reasons, and provide the known effect of not following the standard.

2. Compliance. The report should indicate the nature and extent of compliance testing and disclose immaterial instances of noncompliance. If material instances of noncompliance (either individually or collectively) or questioned cost were found, however, the letter report format would be inappropriate. For instructions on reporting illegal acts or potential illegal acts, see chapter 9.

3. Internal Controls. The report should identify the significant internal controls that were assessed in accomplishing the audit objective, should include the extent of assessment including the control risk, and should disclose any insignificant weaknesses found during the audit. Insignificant weaknesses may be discussed with management and documented in the workpapers rather than included in the letter report. If significant weaknesses were found, this report format would be inappropriate.

4. Privileged and Confidential Information. Relevant information deemed privileged and confidential omitted from the report should be disclosed as follows:

Certain relevant information deemed privileged and confidential has been omitted from this report. This information will be provided on a need-to-know basis to those persons authorized to receive it.

F. FINANCIAL AND FINANCIAL RELATED REPORTS

The reporting requirements for financial audits are contained in the SASs issued by the AICPA and are supplemented by the Yellow Book. These sources, which provide detailed instructions on the composition of financial audit reports, should be strictly followed for financial statement audits. For financial related audits, auditors must make judgments as to which standards apply to the assignment objectives. Restated below are some of the highlights of the additional Yellow Book reporting requirements (see SASs and the Yellow Book for complete details of the requirements) as well as certain other requirements. This section also contains brief discussions of the major financial related reports OA issues.

1. Financial Statement Audits. Reports on audits of financial statements must include the following.

a. Opinion on Financial Statements - A written opinion on the financial statements shall be prepared, including a statement that the audit was accomplished in accordance with generally accepted Government auditing standards. The following language is appropriate to use:

The examination was made according to generally accepted Government auditing standards for financial audits and included tests of internal controls and compliance with laws and regulations to the extent neces-

sary to provide reasonable assurance that the financial statements were free of material misstatement.

If one or more of the applicable standards were not followed, the report should disclose that fact, give the reasons, and provide the known effect of not following the standard.

b. Compliance - A written report on tests of compliance with applicable laws and regulations shall be prepared.

- o The report shall contain a statement of positive assurance on those items tested and negative assurance on those items not tested.
- o The report shall include all material instances of noncompliance, either individually or collectively. (All the finding elements identified should be reported.)
- o An opinion on compliance may be warranted if a valid statistical sample was tested.
- o For instructions on reporting illegal acts or potential illegal acts, see item chapter 9. If the allowability of certain costs is questioned, this fact should be disclosed. Exhibit E in chapter 14 (A:AM14EXE.WPF) provides suggested report language.

c. Internal Controls - A written report on the auditor's understanding of the internal control structure and the assessment of the control risk made as a part of the audit shall be prepared. The report will

- o identify significant internal control structure, including the controls established to ensure compliance with laws and regulations that materially affect the financial statements;
- o identify the scope of the work in obtaining an understanding of the internal control structure and in assessing the control risk; and
- o report "reportable conditions" along with finding attributes identified as a result of the audit, including the identification of any material weaknesses. (The reporting requirement for reportable conditions for financial audits is the same as for performance audits.)

d. Privileged and Confidential Information - Relevant information deemed privileged and confidential that was omitted from the report should be disclosed as follows.

Certain relevant information deemed privileged and confidential has been omitted from this report. This information will be provided on a need-to-know basis to those persons authorized to receive it.

e. Single Document - As indicated above, the reporting standards for financial audits require an opinion on the financial statements, a report on compliance with laws and regulations, and a report on internal controls. These three parts, plus "Other Matters," if used, may be composed separately

or as a single document. Notwithstanding their composition, they should be bound with a common cover and issued as a single document.

The format for the report cover, title page, and table of contents should be the same as for Blue and Buff Cover report formats. For instructions on the composition of the subsequent sections, refer to the SAS as supplemented by the Yellow Book.

For Financial audit reports prepared by IPAs, the issuing regional office shall place an OIG report number on the IPA's standard report cover for transmittal to the cognizant operations office manager.

2. Contract Audit Reports. Most contract audit reports, including those for preaward audits, will be governed by the standard formats prescribed in Part V of this Manual. However, if the findings warrant more formal reporting, the provisions in this chapter will apply.

3. Grant Reports. Depending on the audit objectives, grant audit reports may either follow the guidance provided for Blue and Buff Cover reports (i.e., performance audits) or that provided for financial reports (i.e., financial statement audits or financial related audits). Additional guidance, such as checklists for desk reviews of OMB Circular A-128 reports, is provided in Part VI of this Manual.

4. VANEA Reports. Procedures for preparing VANEA reports are discussed in chapter 22 of this Manual.

EXAMPLE OF TITLE PAGE
BLUE AND BUFF COVER REPORTS

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL

REPORT TITLE, ALL CAPITAL LETTERS

DOUBLE SPACED

CENTERED ON THE PAGE AND UNDERLINED

Report Number: XX-XX-90-01
Date of Issue: Month 1, 199X

____ Regional Audit Office
City, State Zip

-----One-inch Margin-----

EXAMPLE OF TABLE OF CONTENTS
BLUE AND BUFF COVER REPORTS

TITLE OF REPORT IS
ALL CAPITAL LETTERS WITH
EACH LINE CENTERED AND UNDERLINED

TABLE OF CONTENTS

	<u>Page</u>
SUMMARY	X
PART I - APPROACH AND OVERVIEW	X
Introduction	X
Scope and Methodology	X
Background	X
Observations and Conclusions	X
PART II - FINDINGS AND RECOMMENDATIONS	X
1. Finding Title, Single-spaced if More Than One Line Is Needed	X
2. Finding Title	X
PART III - MANAGEMENT AND AUDITOR COMMENTS	X
PART IV - OTHER MATTERS (Optional)	X
Part V - EXHIBITS, APPENDICES (Optional, Becomes Part IV if "Other Matters" are not reported)	

----- One Inch Margin -----

EXAMPLE OF REPORT SUMMARY
BLUE AND BUFF COVER REPORTS

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITS

REPORT TITLE, ALL CAPITAL LETTERS
SINGLE SPACED
CENTERED ON THE PAGE AND UNDERLINED

Audit Report Number:

SUMMARY

The ABC Field Office (ABC) is responsible for supporting the nuclear weapons test programs of the DEF and GHI National Laboratories. This support includes the drilling of test holes for nuclear device testing at the Test Site (TS). The objective of this audit was to assess the effectiveness of the Department of Energy's management of test hole inventories at the TS.

Our audit disclosed that ABC accumulated a large inventory of unused test holes and approved drilling additional holes for which neither laboratory (DEF nor GHI) had identified a need. The overdrilling of test holes occurred because ABC did not comply with good inventory practices that would have had ABC's approving official question the need for, and the timing of, the laboratories' drilling requests. Instead, ABC gave perfunctory approval to the laboratories' work orders for drilling test holes, and emphasized keeping two drill rig crews busy and satisfying the laboratories' demands for dedicated drilling personnel.

Although ABC did not agree that overdrilling had occurred, it has cut back its drilling activities and estimated that this will save about \$7.6 million annually. ABC agreed with the recommendations in the report and has taken corrective actions.

(Authentication, see Chap. 9)

EXAMPLE OF PART I, APPROACH AND OVERVIEW
BLUE AND BUFF COVER REPORTS

PART I

APPROACH AND OVERVIEW

INTRODUCTION

The audit assessed the effectiveness of ... More specifically, the audit objectives were to examine ...

SCOPE AND METHODOLOGY

(Description of scope, methodology.)

The audit was made according to generally accepted Government auditing standards for performance audits and included tests of internal controls and compliance with laws and regulations to the extent necessary to satisfy the objective of the audit.

We assessed the significant internal controls with respect to ... Our assessment consisted of ... Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit.

The firm of JKL, Inc., participated with the Department's Office of Inspector General in conducting the audit. We discussed our findings with the Director of ... and members of his/her staff during an exit conference on Month 1, 199X.

BACKGROUND

(Include background information as necessary to understand issues discussed in the report.)

OBSERVATIONS AND CONCLUSIONS

We found that ... Thus, we recommended that ...

(Actions taken on prior audit reports, if any.)

(Noteworthy accomplishments, if any.)

(Issues requiring further study, if any.)

(Privileged and confidential information, if any.)

Our findings relating to ... (did/did not) disclose any material internal control weaknesses that management should consider when preparing its yearend assurance memorandum on internal controls.

EXAMPLE OF PART II, FINDINGS AND RECOMMENDATIONS
BLUE AND BUFF COVER REPORT

PART II

FINDINGS AND RECOMMENDATIONS

1. Finding Title Upper and Lower Case, Underlined.
(For a single finding, delete the Arabic numeral and center the finding title.)

FINDING

Each finding or "charge" paragraph should be only one paragraph. It should contain (1) criteria, (2) condition, (3) cause, and (4) effect, generally in that order.

RECOMMENDATIONS

The recommendations should immediately follow the charge paragraph, and each cause identified in the charge paragraph should have a corresponding recommendation.

We recommend that the Assistant Secretary for _____:

1. List each recommendation here, and
2. Begin it with an imperative (action) verb.

We also recommend that the Manager, ABC Field Office direct MNO Contractor to immediately implement DOE Order No. 12345.

MANAGEMENT REACTION

Management (concurred/did not concur) with the findings and (agreed/ did not agree) to implement the recommendations.

DETAILS OF FINDING

The "Details of Finding" should, as appropriate, provide brief setup or background narrative as a prelude to the finding. Secondly, the auditor should cite all the applicable criteria. Next, this section should explain the condition as it relates to the cited criteria. Then, it should cite the cause of the condition. Finally, it should cite the effect. This pattern should be repeated for any subfinding within the overall finding, with a summary effect at the end.

Each finding's nature and complexity will require variations on this pattern, but the basic sequence should be followed. Some audit findings, for example, contain several subconditions and effects but only one cause. Re-

stating the same cause each time is needlessly repetitive. Therefore, all the conditions can be cited, then the common cause, then the effects, and finally a summary effect.

Single space all reports that leave the office, including drafts. Double space drafts while they are being written and revised in the office. To help the readers along, indent the first line of each paragraph five characters and separate the paragraphs with one line of white space. Finally, refer to the Government Printing Office Manual for matters not discussed in this Manual.

The format for primary and subordinate captions may vary, but should generally be consistent with the following guidance and examples:

PRIMARY CAPTIONS

Primary captions should be set at the left margin, typed in upper case, and underlined. Two or more captions should be used at each level.

Second Level Captions

Second level captions will also be set at the left margin and underlined, but only the first letter of each major word will be capitalized.

Third Level Captions

Third level captions will be indented five spaces from the left margin. They will also be underlined and the first letter of each major word will be capitalized.

EXAMPLE OF PART III, MANAGEMENT AND AUDITOR COMMENTS
BLUE AND BUFF COVER REPORTS

PART III

MANAGEMENT AND AUDITOR COMMENTS

In responding to our draft version of this report, the [title of person responding] ... [summarize management's comments in one sentence]. A summary of management's comments and our replies follows.

1. Exact Title of Finding 1.

Management Comments. Summarize the management comments here in accordance with the guidance in chapter 10 of this manual. Repeating each recommendation is not necessary unless management does not concur with specific ones.

Auditor Comments. Briefly reply to the management comments here in accordance with the guidance in this chapter.

2. Exact Title of Finding 2.

Management Comments. See above.

Auditor Comments. See above. Continue for each finding.

EXAMPLE OF PART IV, OTHER MATTERS
BLUE AND BUFF COVER REPORTS

PART IV

OTHER MATTERS (OPTIONAL)

1. Use Descriptive Title With First Letter Capital and Underlined.

Normally, this section should be infrequently used because it includes only those findings that do not warrant discussion in the body but are significant enough to be formally communicated as a matter of record. However, no recommendations will be made and a Departmental position is not required for this type of finding. If there is only one matter, the number "1" is omitted from the title and the title is centered.

Whenever this part is not used, the appendices and exhibits become PART IV.

EXAMPLE OF PART V, EXHIBITS AND APPENDICES
BLUE AND BUFF COVER REPORTS

Exhibit A

PART V

EXHIBITS (AND/OR) APPENDICES

Title, Upper and Lower Case
Centered, and Underlined

Exhibits are of two types: (1) Items such as tables, charts, pictures, diagrams, computer printouts, copies of invoices, and other nontext items; and (2) examples of textual documents from other sources, such as copies of letters, memoranda, and pages from other reports.

Appendices contain textual material written by the auditors to supplement the report. This material usually comprises details that are useful information but would disrupt the report's flow. An example would be a discussion of technical detail that explains a finding more fully but is geared to readers with expertise in a specific discipline, such as accounting, computers, or nuclear physics.

Exhibits and appendices are always given the capital letter designations A, B, C, and so on. The word "Exhibit" or "Appendix" appears at the right margin, top of the page. Whenever an exhibit or appendix contains more than one page, the words "Page 1 of X" appear immediately below the word "Exhibit" or "Appendix," with X being the total number of pages to that exhibit or appendix. Exhibits come first, and are followed by appendices.

Whenever Part IV, "Other Matters" is not used in the report, the appendices or exhibits become Part IV instead of Part V.

EXAMPLE OF LETTER REPORT
(USE MEMORANDUM PAPER)

DATE:

Audit Report No.: XX-L-9X-XX

REPLY TO

ATTN OF: IG-XX

SUBJECT: Title of Audit

TO: Auditee

OBJECTIVES OF AUDIT

State the audit objectives here.

SCOPE AND METHODOLOGY

(Description of scope, methodology.)

(Statement on auditing standards.)

(Testing of compliance with laws and regulations, and assessment of internal controls.)

(Contractor assistance, if any.)

(Exit conference.)

BACKGROUND

(Include background information as necessary to understand issues discussed in the report.)

RESULTS OF AUDIT

Describe the results of audit. This section will generally consist of positive observations--e.g., if material internal control deficiencies had been found, a letter report would not be an appropriate vehicle for our findings.

State that since no recommendations are being made in this letter report, a formal response is not required. Also state that we appreciate the cooperation of the auditee staff throughout the audit.

(Name), Manager

Regional Audit Office
Office of Inspector General

cc: Director, Audit Liaison Division (CR-33)

CHAPTER 11REPORT STAFFING AND DISTRIBUTIONA. SCOPE OF CHAPTER

This chapter details the procedures for staffing TF&Rs and draft audit reports, and for distribution of final audit reports.

B. REPORT STAFFING AND DISTRIBUTION POLICY

To ensure that the results of an audit are fairly and accurately reported, management must be provided the opportunity to comment on the audit findings as early as possible in an audit. This process will allow the auditee to provide additional information it feels is necessary to help place the findings in perspective. This process is called "staffing the findings."

Written audit reports are to be timely submitted to the appropriate action officials of the organization audited and to the appropriate officials of the organizations requiring or arranging for the audits, including external funding organizations, unless legal restrictions, ethical considerations, or other arrangements prevent it. Unless restricted by law or regulation, copies should be made available for public inspection.

C. DELEGATION OF ISSUING AUTHORITY

Throughout the remainder of this chapter, authority for issuing various stages of the report are discussed. The issuing authority may be delegated to a lower level. The following matrix shows the lowest level to which the holder of the authority may delegate issuing authority:

Stage of Report	Holder of Authority		Lowest Level of Delegation				
	Blue	Buff	AIGA	RM	ARM	AD	AIC
TF&R	AIGA	RM				Blue	Buff
Official Draft	AIGA	RM			Blue	Buff	
Final Report: Authenticate	AIGA	RM		Blue	Buff		
Transmit	IG	IG		Blue	Buff		

All stages of a Blue Cover report must be approved by AO prior to issuance. As a general rule, memoranda transmitting documents to an assistant secretary or above are signed by the AIGA or the IG.

D. STAFFING THE TF&R

The TF&R should serve as the initial vehicle for discussing tentative findings with the auditee and obtaining written comments. This process is intended to be an integral part of audit verification work and, to the extent possible, should be delegated to the AIC or Audit Director. Procedures for developing and staffing TF&Rs are discussed in more detail in chapter 6.

E. STAFFING THE OFFICIAL DRAFT REPORT

The official draft must also be staffed with management. The requirements for this level of staffing are discussed below.

1. Analysis of Management Comments. After comments on the tentative findings have been received, they are analyzed for inclusion in the official draft report. On those occasions where a Management Alert was issued, it will be used in lieu of a TF&R in terms of incorporating management comments into an official draft.

a. Nonconcurrence With Findings and Recommendations - When management does not concur with the findings and recommendations, a reasonable effort should be made to resolve any differences. When a mutually satisfactory agreement cannot be reached and the finding is still considered valid, an appropriate rebuttal of management's comments shall be included in the report under the "Management Comments" section. This may be done by providing additional information supporting the auditor's view or otherwise showing that management's comments were incorrect. If the auditor cannot effectively rebut management's nonconcurrence, the finding must be changed or deleted. If the comments relate to a question of fact with which we agree, the report should be changed to reflect the correct facts and management's comment omitted.

b. Nonresponsive Comments - The auditor may receive comments that are not responsive to findings, conclusions, or recommendations. In those cases, the auditor should advise management of this fact and attempt to get management to modify its comments so that they are responsive. Failing this, the official draft report should be so noted.

2. Issuing the Official Draft. After management's comments on the TF&R have been analyzed, an official draft report incorporating the written comments received along with auditor comments shall be prepared and furnished to DOE management. Prior to issuance, the official draft shall be referenced pursuant to the procedures provided in chapter 12.

Memoranda transmitting official draft reports to the Assistant Secretary or equivalent level will be signed by the AIGA. Memoranda transmitting official draft reports to officials below this level will be signed by the Regional Manager or designee.

3. Transmittal Memorandum. A transmittal memorandum for draft Blue and Buff Cover reports is illustrated in exhibit A (A:AM11EXA.WPF). All memoranda transmitting official drafts must contain:

- o A statement that the draft has been revised to reflect management comments;

- o Notification that the recipient will be contacted to arrange an exit conference shortly after management has provided its comments on the draft report;
- o A request to provide special handling to avoid premature disclosure outside DOE since the draft does not reflect the final position of the IG; and
- o A statement that the report is subject to DOE Order 2320.2B and requires the formulation of an official Departmental position on OIG reports.

4. Response Time Allowed. The auditee shall be allowed 15 working days to provide comments on the official draft report. Management's failure to provide a timely response to the request for comments on the official draft report should not delay the issuance of the final report except when a requested and justified extension has been granted to the auditee. If a response to the request for comments on the official draft report is not received, that fact should be noted in the final report.

5. Formal Exit Conference. An exit conference will be held to formally discuss the audit results after management has provided its comments on the official draft. Management may elect to waive the exit conference. Additional information on discussing findings with management is provided in chapter 6. Auditors are not precluded from informally discussing draft reports with management prior to the formal exit conference.

F. FINAL REPORT ISSUANCE

Procedures for issuing the final report are discussed below.

1. Final Report Preparation. The final report is prepared after management comments on the official draft have been received. Management comments are analyzed, and the management and auditor comments included in the draft report are revised as appropriate. Performance audit reports are dated as of the authentication date. Financial and financial related audit reports are either dated as of the last day of field work, or they include a statement indicating the last day of field work and that the report has not been updated to reflect events subsequent to that date. A report number is assigned as discussed below.

2. Report Numbering. Report numbers are assigned to all audit reports. The numbers for Blue Cover reports are assigned by AIGP when the report is sent there for printing and distribution. Numbers for all other reports are assigned by the respective regions. These numbers identify the issuing office, type of audit report, fiscal year, and sequential number of that type of report within the fiscal year. Extreme care should be taken to ensure that reports are assigned the correct number. To maintain control over audit reports issued, report numbers will not be assigned until the report is ready for issuance. The issuing office and the type of report are identified by the letters:

<u>Issuing Office</u>	<u>Type of Report</u>	<u>Cover Color</u>
CR - Capital Regional Office	IG - Blue Cover	Blue
ER - Eastern Regional Office	B - Buff Cover	Buff
WR - Western Regional Office	L - Letter	N/A
AP - DAIG/AP ³	C - Contract	Green
IG - Office of Inspector General	P - Preaward	Green
	F - Financial	Green
	G - Grant	Green
	V - VANEA	Orange

For example, the third Buff Cover report issued by the Western Regional Audit Office in Fiscal Year 1993 would carry the number "WR-B-93-3." If the audit was done by a contractor and this was the third Buff Cover report issued based on work performed for us by a contractor, then a "C" should be added to the report number--e.g., "WR-BC-93-3."

3. Executive Summary. An executive summary that summarizes audit results should be prepared to accompany all Blue Cover reports. In general, the executive summary should provide the same information that is included in the Summary in front of each Blue and Buff Cover report. This one-page summary is used by the Secretary for a quick review of the report and will not be included in the final printed report. An executive summary is illustrated in exhibit B (A:AM11EXB.WPF).

4. Final Report Distribution. Normally, only Blue cover reports are distributed to the Secretary. Additionally, all reports are distributed to each DOE official responsible for taking corrective action (officials to whom the recommendations are addressed), other DOE officials, and to other interested parties upon receipt of a valid request.

a. Blue and Buff Cover Reports - Report distribution for final Blue and Buff Cover audit reports shall be made by the AIGP in accordance with procedures established in the OIG Directive IG-200D, "Distribution of OIG Reports," issued 1-7-93. For Buff Cover reports, regional offices should send 10 copies to AO prior to any other distribution. AO will coordinate with the OIG Front Office and advise the regional office as to release of the Buff Cover report to the addressee.

b. All Other Reports - Report distribution for all reports except Blue and Buff Cover follows:

<u>Report Distribution</u>	
<u>Office</u>	<u>Copies</u>
Addressee	2
Audit Liaison	1
AIGA & DAIG/AO	3
AIGI	1
AIG/IA	1
AIGP	1
OIG Regional Offices	1
Audit Groups, as appropriate	1

5. Transmittal and Information Memorandum.

a. Blue Cover - Final Blue Cover reports are transmitted to the Secretary using an information memorandum containing a brief summary of the audit. The information memorandum to the Secretary will be prepared for signature by the Inspector General. Exhibit C (A:AM11EXC.WPF) is an example of the format to be used in the information memorandum, however, the text should be tailored to the specific aspects of the audit. The Blue Cover report is also transmitted to the Department official responsible for taking corrective action (action official). The transmittal memorandum to the action official shall state the requirement for a Departmental position but should not contain a summary of the results, since it is already in the Secretary's transmittal memorandum included with the report (e.g., see exhibit D, A:AM11EXD.WPF).

b. Buff, Financial and Other Reports - Transmittal memoranda for final Financial and other reports are addressed to the DOE official responsible for the audited activity. They contain a brief summary of the audit as well as a request for a Departmental position (e.g., see exhibit E, A:AM11EXE.WPF).

c. Letter Report - Transmittal memoranda are not prepared for letter reports. The reports are addressed to the DOE official responsible for the audited activity.

d. Sensitive or Proprietary Information - If reports contain sensitive or proprietary information they should not be issued as Blue or Buff cover reports as these reports are releasable to any interested party without prior approval of the AIGA.

G. FINAL REPORT PACKAGE

After preparing the report in final form, Regional Managers will forward the final report package to the DAIG/AO. A final report package must be submitted to AO when the report is issued by the region (including Financial audit reports on integrated contractors) or when it is submitted to AO for final review and issuance. This package will include:

- o Three copies of the Final Report (see this chapter and chapter 10 for detail);
- o One copy of the Transmittal Memorandum (see exhibit F, A:AM11EXF.WPF, for an example);
- o One copy of the Monetary Impact Report (see 1 below);
- o Two copies of the Fact Sheet (see 2 below); and
- o One copy of the IGDBMS Audit Project Summary Report (see 3 below).

The signed transmittal memorandum in the package represents the Regional Manager's acceptance and approval of the report and findings contained therein. Whenever the audit work was performed by contractor personnel, all final cost and time information may not be available when the report package is submitted. In these instances, both the Monetary Impact Statement and the Fact Sheet may indicate that data relating to the contractor is preliminary and that final versions of these documents will be submitted when the information is available. Lack of this information should not delay submission of the final report package.

1. Monetary Impact Report (one copy). Although the full impact of AIGA audits, particularly those resulting in increased effectiveness or improved efficiency, cannot be measured, many audit recommendations produce a monetary impact that can be measured and supported. The Monetary Impact Report has been designed to capture and accumulate savings (both program improvement savings and potential recoveries) which can be reasonably measured. See exhibit G (A:AM11EXG.WPF) for an example and detailed instructions.

(a) Computation of Savings - Potential monetary savings will be reported even though the auditee may have disagreed with the findings and recommendations. For summary reports on multi-location audits, DOE-wide savings may be reportable if there is adequate support for a projection. Should a finding summarize the results of reviews at several locations (other than summary reports on multi-location audits), the amount of potential savings reported will be only those that apply to the activities addressed in the finding. For example, in an audit of a function at four sites of a total of 10 locations, the dollar impact will be limited to the four sites visited. An exception to this restriction would be for those cases where statistical sampling techniques are used to project savings or to express an opinion regarding the entire universe from which the sample was drawn. All readily identifiable costs associated with implementing the recommendation and effecting the savings should be considered in computing the net monetary impact.

Implementation costs would include not only those expected to be incurred by DOE activities, but also those of other Government activities. Basically, the savings should reflect the amount contained in the report.

(b) Reporting Potential Savings - Only those potential savings that can be reasonably determined and supported will be reported. Each potential savings reported shall be keyed to a finding in the audit report and the basis of the savings shall be shown in the "Remarks" section (item 7) of the form. All potential savings that will benefit the Federal Government shall be reported, with DOE's portion separately identified. For audit reports that have findings and recommendations but no reportable savings, the "Remarks" section of the form must contain the statement: "Audit report contains no reportable potential monetary impact." The audit workpapers must include explanations of why potential savings could not be determined.

Savings are shown as one time or recurring. One time savings are amounts applicable to only one year. For example, the difference between an alternative expenditure of capital funds that would accomplish the same result as a larger capital expenditure.

Recurring savings occur when the recommendation results in savings in more than one year. The number of years a recurring savings is claimed depends on the nature of the finding. If the number of years is known it should be reported. If the number of years is not known the savings years should be identified as "unknown" and the annual amount reported. For example, savings resulting from an improved procedure would normally be limited to 1 year, since the number of years realized would probably not be known. On the other hand, savings resulting from capital expenditures, such as for machinery, would normally be projected over the life of the asset, not to exceed five years.

(c) Revision of Monetary Impact Report - Additional information may be obtained after the Monetary Impact Report has been submitted. This may come about through DOE management input to DARTS. When this occurs, the additional information will be reviewed by the AIC and the Monetary Impact Report will be appropriately revised.

2. Fact Sheet (two copies). The Fact Sheet provides a synopsis of relevant information pertaining to the audit. This document will be prepared for all audits, including those prepared under contract, by the audit team responsible for the report. See exhibit H (A:AM11EXH.WPF) for an example and preparation instructions.

3. IGDBMS Audit Project Summary Report (one copy). The IGDBMS file should reflect the completion of the audit and be current. In the IGDBMS this report is the APS (audit project summary) and is accessed under AUD (Audit Tracking) using RPT, Menu of Reports option. All data should be complete with the possible exception of OIG time charged, and final billing for contractor costs and time. This information should be updated in the IGDBMS as it becomes available by the auditor in charge of the project. See exhibit I (A:AM11EXI.WPF) for a sample Audit Project Summary Report. The staff day information contained in this report, the Fact Sheet, and the final report package transmittal memorandum should be essentially the same or otherwise explained.

EXAMPLE OF TRANSMITTAL MEMORANDUM OF
OFFICIAL DRAFT FOR BLUE COVER OR BUFF COVER REPORT
(USE MEMORANDUM PAPER)

DATE: Month 1, 199X

REPLY TO

ATTN OF: IG-XX

SUBJECT: Official Draft Report on "Title of Audit"

TO: Auditee

Attached for your review is the subject draft report that reflects management's comments. Please review the report and provide comments within 15 working days on our treatment of your previous comments. We plan to issue the report if we receive no comments by the due date.

The report is subject to DOE Order 2320.2B, "Establishment of Departmental Position on Inspector General Reports," which requires the formulation of an official Departmental position on Office of Inspector General reports. Since this report does not represent the final position of the Office of Inspector General until it is signed and released, you are reminded that the contents shall be safeguarded at all times to prevent improper disclosure. DOE Order 2320.2B prohibits recipients of official draft reports from showing or releasing the contents of the report for other than official review and comment. Official draft reports shall not be provided to anyone outside the Department without the express approval of the Inspector General. In this context, management and operating contractors shall be considered to be part of the Department. However, when official draft reports are given to management and operating contractors, the providing program official is still responsible for ensuring that the document is properly safeguarded. The contractors may only receive the draft reports for the exclusive purpose of aiding DOE in the deliberative process. Further, there is to be no premature release to anyone outside the Department. DOE Order 2320.2B also states that all copies of the report remain the property of the Office of Inspector General and shall be returned on demand.

We appreciate the assistance and cooperation of your staff during this review.

Gordon W. Harvey*
Assistant Inspector General*
for Audits

Attachment

cc:

[* Transmittals of reports to officials below the assistant secretary level may be signed by the regional managers or ARMs, in accordance with the delegation of issuing authority shown on page 11-1.]

EXECUTIVE SUMMARY

Subject: Report on "Audit Testing Laboratory Support to the Environmental Survey Program"

This audit sought to determine whether testing laboratory support for the Environmental Survey Program was performed in accordance with prescribed procedures. A significant part of the program involves the collection and analysis of samples by Department of Energy (DOE) laboratories to test for contamination at DOE facilities. A quality assurance program was established to ensure accurate and valid data results from the tests.

Our review of the Department's compliance with quality assurance standards showed that 43 percent of the laboratory tests on organic samples exceeded standard maximum holding times, and 31 percent of the samples were tested when the laboratories had not qualified, under standard performance criteria, to conduct further tests. Also, deficiencies found by the Environmental Protection Agency were not being corrected. These conditions apparently existed because adequate policies and oversight were not established to ensure adherence to DOE's quality assurance program. Management did not take corrective actions until January 1989, when the analysis program was essentially complete.

The primary concern of the report is securing credible results in future testing endeavors. Management believes that several factors will mitigate the sampling and analysis problems noted in our report.

EXAMPLE OF INFORMATION MEMORANDUM TO
THE SECRETARY FOR BLUE COVER REPORT
(USE MEMORANDUM PAPER)

DATE: March 23, 199X

REPLY TO
ATTN OF: IG-1

SUBJECT: INFORMATION: REPORT ON "Followup on Audits of Purchase of Natural
Gas Pipeline Lease"

TO: The Secretary

BACKGROUND:

In April 1990, the Office of Inspector General issued two reports, ...that criticized the Department for paying excessive costs to purchase and transport natural gas and for leasing its pipeline at less than fair market value. We conducted this followup audit to determine if the Department....

DISCUSSION:

The Albuquerque Operations Office did not follow the course of action recommended, which we believe, would have produced annual savings of about \$3.6 million. Specifically, This occurred because Albuquerque had not assigned responsibility for administering the lease. Thus, we recommended that....

The Albuquerque Operations Office agreed with our findings and recommendations.

John C. Layton
Inspector General

Attachment

cc: Deputy Secretary
Assistant Secretary for Defense Programs
Director, Office of ... (as appropriate)

EXAMPLE OF TRANSMITTAL MEMORANDUM OF
BLUE COVER REPORT TO ACTION OFFICIAL
(USE MEMORANDUM PAPER)

DATE: Month 1, 199X

REPLY TO

ATTN OF: IG-XX

SUBJECT: Report on "Title of Report"

TO: Assistant Secretary for ...

Attached is the subject report. In accordance with DOE Order 2320,2B, "Establishment of Departmental Position on Inspector General Reports," the Department is requested to provide a Departmental position on the recommendations contained in the report.

Paragraph 8.f. and Attachment 1 of the directive describe the procedures for preparing and processing the Departmental position. The reply is due to the Chief Financial Officer 70 days from the date of the report.

We appreciate the cooperation of your staff during the review.

John C. Layton*
Inspector General*

Attachment

cc: Director, Audit Liaison Division (CR-33)

[* Transmittals of Blue Cover reports to officials below the assistant secretary level may be signed by the AIGA or regional managers.]

EXAMPLE OF TRANSMITTAL MEMORANDUM OF
BUFF COVER REPORT AND FINANCIAL AUDIT REPORT

DATE: Month 1, 199X

REPLY TO

ATTN OF: IG-XX

SUBJECT: Report on "Title of Audit"

TO: Appropriate DOE Official

We audited (subject and location). The specific objectives of the audit were to determine whether ...

The audit disclosed ...

Your comments on the draft report indicated (concurrence or nonconcurrence) with the recommendations. The details of management and auditor comments are set forth on pages ... of the report.

In accordance with DOE Order 2320.2B, "Establishment of Departmental Position on Inspector General Reports," the Department is requested to provide a Departmental position on the recommendations in the report. Paragraph 8.f and Attachment 1 of the order describe the procedures for preparing and processing the Departmental position. The reply is due to the Chief Financial Officer 70 days from the date of this report.

We appreciate the cooperation of your staff throughout this audit, including the attention given to resolving the findings in the report.

(Name), Manager

Regional Audit Office
Office of Inspector General

Attachment

cc: Director, Audit Liaison Division (CR-33)

EXAMPLE OF TRANSMITTAL MEMORANDUM FINAL REPORT PACKAGE
(USE MEMORANDUM PAPER)

DATE: Month 1, 199X

REPLY TO

ATTN OF: IG-XX

SUBJECT: Final Report Package for "Title of Audit"

TO: (Name), DAIG/AO

Attached is the required final report package on the subject audit. The pertinent details are:

1. Staff days: Programmed _____ Actual _____

(Explanation for difference)

2. Elapsed days: Programmed _____ Actual _____

(Explanation for difference)

3. Names of OIG audit staff:

Assistant Regional Manager:

Audit Director:

Auditor-in-Charge:

Audit Staff:

4. Names of Contractor audit staff, if any:

Audit Director:

Auditor-in-Charge:

Audit Manager:

Audit Staff:

4. Matters to be brought to attention of the IG or AIGA:

(Name), Manager

_____ Regional Audit Office

Office of Inspector General

Attachments:

1. Final Report (3) (Other than blue cover report)
2. Executive Summary (2) (Blue cover report only)
3. Monetary Impact Report
4. Fact Sheet (2)
5. IGDBMS File Printout

MONETARY IMPACT OF REPORT NO.

1. Title of Audit: _____

2. Region/office: _____

3. IGDBMS No. : _____

4. Type of Audit: (Definitions and examples of audit types are found in the Yellow Book, pages 2-1 thru 2-5.)

Financial

Performance

Financial Statement

Economy and Efficiency

Financial Related (Specify

Program Audits _____

type) _____

5.

FINDING		BETTER USED			QUESTIONED COSTS			MGT. POSITION	POTENTIAL BUDGET IMPACT	
(A) No.	(B) Title	(C) One Time	(D) Amount Per Year	(E) No. Yrs.	(F) Total Amount	(G) Ques- tioned Portion	(H) Unsup- ported Portion	(I) Total	(J) C=Concur N=Noncon U=Undec.	(K) Y=Yes N=No
TOTALS--ALL FINDINGS									XXXXXXXX	XXXXXXXXXX

6. Remarks:

7. Contractor

10. Approvals:

8. Contract No.

Regional Manager _____

9. Task Order No.

DAIG/AO _____

Instructions for Preparing Monetary Impact Report

This report provides a synopsis of the monetary impact pertaining to the audit. The dollar amount of the saving (s) contained in the monetary impact report should tie directly to the audit report. The monetary impact report will be prepared by the audit team responsible for the report for all audits, including those prepared under contract. Add the report number to the heading and use the following instructions in completing the remainder of the form.

1. Title of Audit. The complete report title as it appears on the report cover.
2. Region/Office. The identity of the region and the audit office.
3. IGDBMS Number. Enter the assigned number.
4. Type of Audit. Check the type and sub-type as appropriate. If Financial was checked, indicate in the Remarks section if this was a certification of the financial statements.
5. Matrix. This item is designed to collect various information related to the details of the reports. The monetary impact of financial, performance and certain financial related audits should be classified as "better used" and/or "questioned cost" as appropriate. Instructions for each column follow:
 - a. Number and Title of Findings (Col A and B) - The number, of course, applies to multi-findings reports and reflects the sequential number assigned to the individual findings in the body of the report. The title of the finding will be the exact language used for the heading of the finding.
 - b. Better Used (Col C thru F) - The amount of estimated cost avoidances or increased efficiency or effectiveness which can be realized if DOE managers adopt and implement the audit recommendations to improve their operations or systems. These savings could result in deobligation of funds in the current year and/or budgetary reduction in future years. Note that "better used" amounts have not been spent.

Column C: The estimated amount of savings that can be achieved one time by implementing the recommendation. Note that the impact of preaward audits (both questioned and unsupported) should be entered in this category as separate entries with each amount identified as either (Q) for questioned or (U) for unsupported.

Column D,E,F: The estimated amount of recurring savings that can be achieved yearly. If life expectancy of the audited entity cannot be identified, use one year. If the life can be determined, use the life expectancy up to five years.

- c. Questioned Costs (Col G thru I) - An incurred cost is questioned because (1) of alleged violation of a provision in the law, regulation, contract, grant, or cooperative agreement; (2) lack of adequate documentation to support the cost, (3) it is not allocable to Government work on the basis of benefits received; or (4) the expenditure of funds was unnecessary or unreasonable.

Note that questioned costs based on any of the above four reasons resulting from performance audits of operations being performed by DOE contractors should be reported in this category. Also Note that "questioned" amounts have been spent.

Column G: The costs that are questioned because of reasons (1), (3), and (4) of the above paragraph. Note that in general recommended recoveries from performance audits should be included in this sub-category identified with a (R) at the end of the amount.

Column H: Incurred cost that is questioned because such costs are not supported with adequate documentation and should be in the subcategory "Unsupported," as required by the IG Act of 1988.

Column I: The sum of G and H.

- d. Management Position (Col J) - This column will be used to reflect management's concurrence (C) or nonconcurrence (N) with the amounts being reported. If known, please indicate the amount being reported that management disagrees with.
- e. Budget Impact (Col K) - A determination whether the monetary impact can be potentially be used to reduce current or future years' budgets. In general, the potential amount to be reduced should come from the "Better Used" category.
6. Remarks. This section shall be used to provide any additional pertinent information regarding management's position and to bring to the attention of Headquarters any matters of special importance regarding the monetary impact.
7. Contractor. If the audit was done by an audit services contractor, the name of the contractor will be entered on this line.
8. Contract No. The number of the contract under which the work was done will be entered on this line.
9. Task Order No. The specific task order authorizing the contractor to do the work will be entered here.
10. Approvals. Designated officials and signature of approval.

FACT SHEET
AUDIT REPORTS SUBMITTED TO AIGA

1. Type of Report
 Blue Cover _____
 Buff Cover _____
 Letter _____
 Other (Specify) _____

2. Report No. _____
 3. IGDBMS No. _____
 4. Date Issued _____
 5. Audit Category _____
6. Title: _____

7. Location of Contractor or Activity: _____
8. Audit done by: AIGA _____ IPA _____ Cost _____ E or F _____
9. Type of Audit:
 Financial _____ Performance _____
 Financial Statement _____ Economy & Efficiency _____
 Financial Related (Specify Type) _____ Program Audit _____
10. Coordination with Investigations:
 Discussed with _____
 Date _____
 Disposition:
 No investigative potential _____
 Referred to _____
 Date of Referral Memo _____
11. Workpaper and Report Quality Control:
 W/P Review: AIC _____ Date: _____ Audit Dir.: _____ Date: _____
 Report Ref: Initial: _____ Date: _____ Final: _____ Date: _____
12. Savings:

Better Used				Questioned Cost Incurred			Poten. Budget Impact
One Time	Recurring		Total Amount	Questioned Portion	Unsup-ported Portion	Total	Y=Yes N=No
	Amount Per Year	No. Yrs.					

	OA		Contractor (IPA)	
	Staff Days	Elapsed Days	Staff Days	Elapsed Days
13. Original Program	_____	_____	_____	_____
14. Revision (Date: _____)	_____	_____	_____	_____
Revision (Date: _____)	_____	_____	_____	_____
15. Actual	_____	_____	_____	_____
16. Difference (13-14)	_____	_____	_____	_____
17. Total Days Suspended	_____	_____	_____	_____

18. Explanation of Overruns in Staffdays and/or Elapsed Days, and Suspensions:

19. Project Cross-Indexing:

a. _____	k. _____
b. _____	l. _____
c. _____	m. _____
d. _____	n. _____
e. _____	o. _____
f. _____	p. _____
g. _____	q. _____
h. _____	r. _____
i. _____	s. _____
j. _____	t. _____

(Enter key words on additional page, if necessary.)

20. Narrative of Report:

21. Submitted By: _____ Date: _____

22. AO Review By: _____ Date: _____

Instructions for Preparing the
Audit Report Fact Sheet

The Fact Sheet provides a synopsis of relevant information pertaining to the audit. It will be prepared for all audits, including those prepared under contract, by the audit team responsible for the report. The following instructions apply:

1. Type of Report. Check the appropriate line identifying the type of report being submitted.
2. Report No. Enter the report number assigned.
3. IGDBMS No. Enter the assigned job number.
4. Date Issued. Enter the date on the report.
5. Audit Category. Enter the major audit category as described in the IGDBMS Manual.
6. Title. Enter the complete title as it appears on the report cover or as identified in a Letter report.
7. Location of Contractor Activity. Enter the geographical location(s) where the audit was actually performed.
8. Audit done by: AIGA ____ IPA ____ Cost ____ E or F _____. Enter the name of the regional office or the name of the IPA who performed the audit. In cases where both AIGA and IPA personnel performed the audit, identify all AIGA regions and IPA firms involved. Enter the total task order(s) cost associated with the work performed on the audit. Costs will include all presurvey/survey efforts pertaining to the resultant audit. If final cost are available indicate "F;" if final costs are not available, enter "E" for estimated and use the latest actual billed amount plus an estimated for the unbilled portion.
9. Type of Audit. Check the appropriate line or identify the type of audit if "Other" is checked.
10. Coordination with Investigations. Based on this discussions with AIGI staff, enter the determination made that (1) release will not compromise possible investigations, or (2) the report was referred to AIGI staff for further review. If the report is referred, that fact should be documented by a referral memo. Enter the addressee and date of the referral memo.
11. Workpaper and Report Quality Control. Enter the name of the workpaper reviewer, report referencer, and dates when review was accomplished.
12. Savings. Enter the data from the total line of item 5 on the Monetary Impact Report.

13-18.

These sections indicate the planned and actual staff days (both AIGA and contractor) for the job. If overruns were incurred or the job was suspended, detailed explanation of the reasons for the conditions should be provided. The information is important to AIGA management; therefore, care must be taken to record and accumulate the data consistently and correctly. Elapsed days are calculated from the entrance conference date through the report date. Data should agree with Audit Project Summary Report.

19. Project Cross-Indexing. Enter key words and phrases associated with the project. Examples: "Acme Corporation," "Jones," "Fraud," and "Grant," etc. At the inception of an audit, this information shall be loaded into the IGDBMS. Upon completion of the audit, this information must be updated by the regional office.
20. Narrative of Report. The basic purpose of the narrative is to summarize the audit for OIG management. Therefore, this section must be concise and complete in all factual matters. For a contract, preaward or grant audit, indicate the type of audit, what goods or services are being purchased, the amounts of questioned, unsupported and/or unresolved costs, and the general basis for such a determination. For all other audits, indicate what was audited and provided sufficient information on each finding, including recommendations and monetary impact, for a reader unfamiliar with the subject to understand what was found.
21. Submitted By ____ Date _____. Name of the responsible audit manager who prepared the fact sheet and the date prepared.
22. AO Review By ____ Date _____. To be added by the AO staff member who reviewed the report and related fact sheet.

**OFFICE OF THE INSPECTOR GENERAL
AUDIT PROJECT SUMMARY REPORT (APS)**

11/24/93

Audit-No:	A93PR036	Title: BNL ADMINISTRATION OF SDB PROGRAM		
Milestones:		PLANNED	REVISED	ACTUAL
	PROFILE	END OF SURVEY		
ENTRANCE CONFERENCE:	01-OCT-92	02-DEC-92	02-DEC-92	02-DEC-92
SURVEY COMPLETED:	04-DEC-92	05-FEB-93	05-FEB-93	05-FEB-93
TF&R'S ISSUED:		14-JUN-93	10-AUG-93	10-AUG-93
DRAFT REPORT ISSUED:		02-AUG-93	10-AUG-93	10-AUG-93
EXIT CONFERENCE:		18-AUG-93	10-AUG-93	10-AUG-93
COMPLETED WITH REPORT:	30-AUG-93	30-JUL-93	30-JUL-93	25-AUG-93
ELAPSED DAYS:	333	240	240	266
STAFF DAYS:	150	130		210

DATE SUSPENDED:		DATE TERMINATED:	
DATE REACTIVATED:		DATE CANCELLED:	
NO OF DAYS SUSPENDED:		REPORT NUMBER:	ER-L-93-09

***** AUDIT CODES AND PERSONNEL *****

IG-OFFICE:	PRA PRINCETN AUD	TASK-NO:	-
AUDIT-TYPE:	EAE ECONOMY & EFFICIENCY		
CATEGORY:	MPA MULTIPROGR. ACTIVITY	AD:	115 STRONCZER
DOE-ORG:	CHO CHICAGO OPERATIONS O	AIC:	444 BOZARTH
MAJ-ISSUE:	009 PROCUREMENT AND GRAN	HDQ-MON:	544 ACTON
SITE:	SSA SINGLE-SITE AUDIT	ARM:	101 CONNOR

***** ATC INFORMATION *****

ATC	Rank	ATC Description
B01A	1.0	THE CONTRACTORS PROCUREMENT PRACTICES ARE IN ACCORDANCE WITH

***** FACILITY/LOCATION INFORMATION *****

Code	Description	Location
BNL	BROOKHAVEN NATIONAL LABOR	BROOKHAVEN NATIONAL LABORATORY, NY

***** TASK INFORMATION *****

TASK-ORDER-DATE:	CO TECH. REP:
ORIG-AUTH-HOURS:	ORIG-AUTH-COSTS:
CURRENT-AUTH:	CURRENT-AUTH-CST:
TOT-ACTL-IPA-HR:	TOT-ACTL-COST:

***** TIME CHARGES *****

Emp/Cont Name	No.-Days	Last-Date	Emp/Cont Name	No.-Days	Last-Date
BOZARTH	125.6	30-OCT-93	STRONCZER	13.8	30-OCT-93
CONNOR	1.3	04-SEP-93	FLYNN	52.4	04-SEP-93
TERZINI	12.8	15-MAY-93	SIMPKINS	1.3	20-MAR-93
NARLIS	3.1	26-DEC-92			
TOTAL:	210.3				

CHAPTER 12ASSURING A QUALITY REPORTA. SCOPE OF CHAPTER

This chapter sets forth the policies and practices for assuring that OA issues quality reports.

B. REVIEW OF WORKPAPERS

General procedures for workpaper review are provided in chapter 7. However, procedures of particular importance include the following.

1. The AIC responsible for the assignment should review all workpapers for compliance with OA standards and prescribed procedures--before supervisory review and referencing begins--to assure that all papers are properly prepared and cross-indexed and the work has been adequately accomplished. AICs should indicate their review by initialing and dating the papers.

2. Workpapers should be reviewed by the AIC's immediate supervisor, usually an Audit Director. An ARM should provide this review if the Audit Director is the AIC. As a minimum, the supervisor should review sufficient workpapers to express an opinion on the adequacy of the workpapers (see also chapter 7). The supervisor's review should be made before the report is referenced and the exit conference. The supervisor's comments should be recorded on a review sheet, signed, and dated. All review notes should be retained as a part of the working paper files.

C. REVIEW OF REPORTS

The report review function is performed by Audit Directors, and Regional and Headquarters staff, and is essential to the overall quality of an audit report.

1. Regional Review. Effective supervisory review by the audit director and regional staff is essential to the overall quality of an audit report. Early supervisory participation in the audit planning process helps to focus and sharpen the audit objectives and thus the reporting objectives. Generally, the supervisor can provide a broader perspective on such matters as the reasonableness of the objectives in view of OA policies and practices and the anticipated reaction to the report by various auditees. As the audit progresses, supervisory input may help to determine the type of report to be issued and assist in identifying additional data needed to substantiate and refine the findings, or to sharpen recommendations. Supervisory agreement is required in making the final decision on whether, and to what organizational level, the report will be issued (see chapters 4, 6, and 7.)

2. Headquarters Review. Reports which are to be forwarded to Headquarters for review prior to issuance include

- o All stages of Blue Cover reports (including TF&Rs);

- o Draft reports specifically designated by the AIGA, including all draft reports of a critical/sensitive nature, i.e., congressional interest, significant public interest, or national security implications, and
- o All Management Alerts.

The purpose of the Headquarters review is to ensure (1) quality reports, (2) continuity and consistency of reports and recommendations, and (3) compliance with OA and OIG reporting policies. The Reports Review Checklist, shown in exhibit A (A:AM12EXA.WPF), will be used in the Headquarters review process. All review comments will be coordinated with the DAIG/AO, who will inform the appropriate Regional Manager of any questions or suggested changes to be made to the report. Any difference of opinion between the Regional Managers and Headquarters will be resolved as quickly as possible. When a satisfactory agreement cannot be reached, the matter will be referred to the AIGA for resolution.

3. Documenting Changes Made by Reviewers. Where report drafts are significantly changed as a result of Regional or Headquarters review, the reasons for such changes must be documented in the workpapers. Where applicable, the workpapers should contain reference to relevant audit standards. For example, if the Scope and Methodology section of a Blue Cover report is changed by a Headquarters reviewer to more closely adhere to Yellow Book standards, a notation to that effect should be included in the workpapers. This process assures that there is a documented rationale for significant changes from one draft to the next.

D. CROSS-INDEXING REPORTS

The AIC should follow specific steps in preparing a report for referencing.

1. Workpaper and report cross-indexes are to be placed on reports by the person who prepares the report. The AIC is responsible for ensuring that all portions of the report have been properly cross-indexed.

2. To the extent practicable, specific supporting evidence in the workpapers is to be identified by placing a single vertical line in the margin of the workpaper along side the evidence. Also, "highlighting" or "underlining" may be used. In any event the auditor should cross-index material to the report with a capital "R" or stating "To Report."

3. A workpaper cross-index should be repeated where there is one or more intervening cross-indexes.

4. All cross-indexes will normally be to a specific page of a workpaper--e.g., A1, p. 1. If it is necessary to cross-index a statement (sentence or phrase) to more than one workpaper or to more than one page in a workpaper, the specific pages should be identified--i.e., A1, pp. 1 & 6, not A1-A6.

5. The report cross-index should be placed directly opposite the statement to which it relates. Lines may be drawn across the page to delineate where the statement begins and ends to which the cross-index applies.

6. All figures, amounts, dates and titles appearing in the report must be supported by identical figures or amounts in the workpapers. Also, a referencer should not have to perform computations to determine how a reported figure was computed. For example, in support of a statement that "four of the seven (57 percent) T&A reports did not have the required attachments," the cross-index may be referred to such entries as;

- o 3 reports had the required attachments, and
- o 4 reports did not have the required attachments.

However, the referencer should not have to add the "3" and "4" to get support for the "7." That calculation should be reflected in the workpapers. Likewise, the workpaper should contain computations for "57 percent." Normally, calculations should be carried out to a greater degree of accuracy than the figure cited in the report--e.g., $4 / 7 = 57.1$ percent (rounded) = 57 percent. In addition, a separate cross-index would be needed to support that the attachments were "required."

7. Whenever factual material is repeated in a draft report, it is desirable to cite other pages in the report for support rather than repeatedly citing the same supporting workpapers. This situation may frequently occur in the "Finding" paragraphs where the same information is normally repeated under the "Details of Finding." Likewise, material in the "Observations and Conclusions" section of a report may be the same as that in "Finding" paragraphs. Citing other pages with the same information allows the referencer to carry forward the referencer's mark on material already verified. It may also aid in identifying redundant statements.

8. Auditors should avoid citing a large number of cross-indexes to support a single statement. If several cross-indexes are needed to support a statement, a separate workpaper summary should be prepared which ties together the various pieces of information needed to support a finding or conclusion. However, the workpaper summary must be cross-indexed, factual items traced to source, and computations verified.

E. REFERENCING

The referencing process is another essential step in assuring overall audit report quality. Referencing is defined as the verification of factual data, the determination of the reasonableness of the conclusions reached in view of the factual data provided, and the practicality of the recommendations made in an audit report. All audit reports will be independently referenced. Where administratively feasible, referencing will be performed by an audit staff member who is grade GS-12 or above. For Blue Cover Reports or other reports with significant or controversial findings, preferably, an auditor at grade GS-13 or above should be selected as the referencer. The referencer must not have any management responsibility for the audit nor have participated in the audit. The purposes of referencing are:

- o To verify the accuracy of all facts stated in the report and make a determination as to whether the working papers adequately support the findings, conclusions and recommendations; and
- o To review the soundness and clarity of the report's presentation.

Referencing is to be completed before the official draft report is staffed (see chapter 11) within the Department. (Do not reference the TF&R, which is issued before the official draft.) Referencing does not relieve supervisors of their responsibilities for reviewing workpapers or determining whether the report complies with all prescribed reporting policies and requirements.

The following matrix summarizes the versions of the report requiring cross-indexing and referencing.

<u>Before Release Of</u>	<u>Document Must Be</u>	
	<u>Cross-Indexed</u>	<u>Referenced</u>
TF&R	Yes	No
Official Draft	Yes*	Yes
Final Report*	Yes*	Yes*

- * Only those changes made after the official draft was referenced.

The referencer represents the Regional Manager, who is responsible for the report. The referencer, although not responsible for the report itself, is responsible for determining that:

- o Every figure and statement of fact is supported by satisfactory evidence in the workpapers or by mathematical or clerical checks. This includes:
 - Checking each figure and statement of fact for consistency within the report and to the supporting workpapers; and
 - Independently verifying the accuracy of each total, percentage or similar figure in the report.
- o The report findings, conclusions and recommendations are logical, sound, clearly presented and adequately supported by workpapers.

1. Referencing Documentation. At the start of the referencing process, the referencer will be given a completely cross-indexed copy of the report and all supporting workpapers.

The referencer should use the updated version of Referencer's Review Sheets and is encouraged to use word processing techniques when filling out

the sheets with reference comments (see exhibit B, A:AM12EXB.WPF). These sheets serve as a record of the comments raised by the referencer, their consideration by the audit staff, and their final disposition. The referenced report and the Referencer's Review Sheets should be retained in the workpapers.

2. Referencing Procedures. Referencing consists of three distinct phases. These are: (1) general familiarization with the report to be referenced and the underlying support; (2) detailed referencing; and (3) resolution and disposition of the comments raised during the referencing process.

a. General Familiarization - The referencer should first scan the underlying source material to obtain a general understanding of the organization of the workpapers.

The general familiarization phase provides referencers with the opportunity to identify any restrictions that will affect the referencing process and will necessarily qualify their work. For example, certain support may not be available in the workpapers since it is to be provided by a headquarters branch or another regional office. These restrictions should be noted by the referencer on the Referencer's Review Sheet. However, they must be resolved before the referencing is complete.

b. Detailed Referencing - During the detailed referencing phase, the referencer checks every fact, figure, date, title, etc., in the written product to the underlying support to determine its accuracy and to ensure that it is consistently used.

(1) Important items of information in the report--contract numbers, quotations, dollar amounts, interpretation of contract terms, paraphrasing of policy, law, or regulation, etc.--should be checked to copies of the original source documentation in the workpapers.

(2) The referencer's review is independent and based on the referencer's own knowledge and logic. The referencer should question the adequacy of supporting documentation included in the workpapers when warranted regardless of supervisory review. If the opinions, conclusions and recommendations are not consistent with the factual material examined, which received supervisory review, the referencer should record his/her dissenting view.

(3) Lead schedules and summaries may be used as support if the information on them has been cross-indexed and traced and verified to the original source. The referencer should trace selected items to the source indicated to assure that the information is factual and correct. To the extent that the referencers test workpaper summaries and lead schedules, they should "tick" off on that information the same as for the report being referenced.

(4) The referencer should indicate acceptance that each sentence of the report is supported by placing a referencer's tick mark (") at the left-hand margin of each line (see exhibit C, A:AM12EXC.WPF). Every figure, date, proper name, title, address, and each word of a quotation will

be referenced by placing a tick mark (~) immediately over it. In addition, each handwritten word inserted must be ticked. The referencer should use a different color pencil than was used for indexing or by other reviewers.

(5) All computations should be checked by the referencer and marked (~) to indicate that the computation has been independently verified.

(6) Material referenced only to an interview will require qualification in the report by a phrase such as "we were informed", depending on the circumstances.

(7) The referencer should record all points, questions and suggestions on a Referencer's Review Sheet, spaced so that comments on the disposition can be made without crowding (see exhibit D, A:AM12EXD.WPF).

The suggested way of cross-indexing comments on the review sheet to the report is to place the report page number and the referencer's symbol (a circled 1, 2, 3, etc.,) on the Referencer's Review Sheet opposite the comment. The referencer's symbol is then noted on the report next to the statement relating to the comment, as illustrated in exhibit D (A:AM12EXD.WPF).

(8) The referencer should verify that adequate support is contained in the workpapers for all reported facts. The referencer should scan each workpaper cited as support to see if there are any conditions or qualifications that would affect the validity of the workpaper. All references must be to the workpapers, including copies of pertinent sections of documents, published reports, or other published documents. For example, if DOE Order 2100.1A is cited as support, the appropriate pages should be copied and placed in the workpapers. When support for a reported fact is not located in the cited workpapers, the referencer should immediately write a reference note and proceed with the remainder of his review.

(9) The referencer should not normally spend time searching through the workpapers if a cited reference does not provide the needed support. However, if referencers are aware that an uncited workpaper may contain the needed information, they should note this in their reference note (e.g., their note may state that a particular fact is not supported by the cited reference, and identify the specific workpaper that may contain the needed information).

(10) When referencing classified material, referencers should check the classification of each paragraph to the source documents unless the audit staff plans to have the Department reclassify the draft at a later date. In the latter case, referencers should note in their comments that they have not verified the classifications. Referencing comments should also be classified as appropriate for proper security.

(11) In referencing computer-generated data, the referencer has two major considerations: (1) How far to go in referencing computer programs written by OIG staff; and (2) the extent to which the reliability of computer-generated data should be assessed.

(a) The use of microcomputers and computer programs does not lessen the referencer's responsibilities. Most standard referencing procedures will apply.

- o An audit trail must be provided so that report data can be traced back to the supporting source data.
- o The working papers should fully document the procedures, computer programs and micro coding.
- o When applicable, data on floppy disks used in the audit should be included as part of the working papers and should be properly referenced.

Additionally, referencers must assure that computer instructions developed by OIG staff and used on the assignment are fully documented and have been reviewed for appropriateness and accuracy.

(b) The audit staff must make a reliability assessment (see chapter 8, "Advanced Audit Techniques") when:

- o Computer generated data or information is an integral part of the auditee's operations being audited; or
- o Computer products or outputs are to be used in a report or in support of a finding.

Reliability assessments may entail additional verification with computer-generated data or tests of reasonableness. The referencer's responsibility in this area is to:

- o Verify that a reliability assessment was made; or
- o Make sure that appropriate qualifying language is included in the "Scope" section of the report if a reliability assessment was not adequately made.

If an assessment was not adequately made, and the Scope section not qualified, referencers should point this out in their referencing comments.

(12) Reports published by the OIG may be used as support for items being referenced if that information is historical or not subject to change.

(13) In sensitive cases, material referenced only to a record of an interview may require qualification by a phrase such as "We were informed" depending on the circumstances. The referencer must use judgment concerning whether the support is adequate to make an unqualified statement. This would depend on the source of the information, the source's position, the source's probable knowledge of the subject, and confirmation by others.

(14) The referencer is responsible for ensuring that all factual information is appropriately identified and supported. Any information identified as an "opinion" or "conclusion" should be checked to

ensure that it does not include any elements of fact which would require direct workpaper support. Likewise, all conclusions should be evaluated against factual material in the report to ensure that "cold" readers would reach a similar conclusion based on the same facts.

(15) Where material is supported only by interview evidence, the referencer will check to determine whether the support is adequate to make an unqualified statement. This would depend on the source of the information; the source's position and, therefore, the source's probable knowledge of the subject; and collaboration by others. In some cases, the statement may have to be modified by "We were told" or "We were informed." Also, the referencer should watch for statements that may not be true, even if attributed to a source (i.e., is the source credible?). The OIG should not be repeating potentially untrue statements, even if the statements are attributed to a source.

(16) The referencer is responsible for suggesting editorial changes, such as grammar, punctuation, misspelled words and choice of words, only to the extent that meanings need to be clarified in order to properly discharge the referencing duties. It is, however, within the referencer's duties to comment on OA standards and procedures, such as reporting formats, scope statements, internal controls, data reliability, and other requirements, addressed in this manual.

(17) If the report contains any figures carried forward from a preceding report--e.g., a financial statement audit--such figures should be cross-indexed and referenced to the previous report to assure that they are in agreement. If differences appear, they must be explained in the report.

3. Resolution and Disposition of Referencing Comments. Once the detailed referencing has been completed, the audit staff must consider each referencing comment, record the proposed disposition on the Referencer's Review Sheets, and return the package of material to the referencer. The audit staff should clearly indicate on the review sheets whether they accept, modify or reject the referencer's comments (see exhibit D, A:AM12EXD.WPF). The referencer reviews the disposition made by the audit staff. If satisfied with the disposition, the referencer indicates approval by initialing, dating, and checking off "OK" on the Referencer's Review Sheet. The referencer must also initial, date, and tick the applicable line or item in the report (see exhibit C, A:AM12EXC.WPF).

a. If additional source material has been provided in response to a comment, the referencer makes sure that the additional material is added to the working papers and references to the additional sources have been added to the left-hand margin of the report pages. If the disposition involves a revision to the report, the referencer must check and, when satisfied, place a reference mark on the revised material.

b. Frequently, the referencer and audit staff will discuss the comments raised and their disposition. Oral explanations by the audit staff often provide clarification for the referencer. The referencer should keep in mind, however, that all facts must be supported by written material in the

workpapers. Therefore, oral explanations alone will not suffice. The fact that an explanation was needed may indicate the need to clarify the report or to revise the supporting workpapers.

c. If the referencer and the audit staff cannot agree on the disposition of a comment, the audit staff will write, on the review sheet, a brief explanation of the reason for rejecting the comment, pointing out the differences that generated the disagreement.

d. The "open" points will be brought to the attention of the ARM, who will meet with the referencer and the audit staff to resolve the matter. Only the ARM or higher level official can close a point without resolution. This action is indicated by writing "pass" and inserting their initials in the disposition column. Referencers have the right to appeal to the Regional Manager if they disagree with the ARM's decision.

4. Revisions To Referenced Reports. Changes made to a report after referencing, including changes to the auditee comments in the final report, must be shown to the referencer so they can be referenced. If changes have been made, the referencer will reference the new report. In this case, the changes made to the report will be referenced, and the referencer should determine whether these changes affect other previously referenced sections of the report.

The unchanged material should be indexed to the prior referenced report. To accomplish this, the page number of the prior report can be inserted in the left margin by the referencer.

New material will be referenced as usual with workpaper sources added to the left margin. Index symbols supporting changed material, as well as the related reference marks, should be in the same color as in the first referencing.

REPORTS REVIEW CHECKLIST

Audit Name: _____ Assignment No: _____
 Finding Title: _____ Reviewer: _____

FINAL REPORTS

Yes No Note

1. Report cover & title page prepared correctly.
3. Table of contents format & page references correct.
4. Other Matters are brief, needed, relevant, and clear.
5. Exhibits/appendices correct and appropriate.
6. All transmittal memoranda prepared.
7. Fraud/illegal acts, report cleared for issuance.
8. Audit report package submitted with final report.

REPORT SUMMARY - draft & final reports

1. Identifies activity/entity audited.
2. General purpose of the audit stated.
3. Brief description of major finding(s).
(Summary should generally not exceed one page.)
4. Management reaction.
5. Authentication.

PART I - APPROACH AND OVERVIEW - draft & final reports

1. Purpose and Objectives - Describes detailed audit objectives.
2. Scope and Methodology
 - a. Describes universe, what was audited, & statistical sampling method used.
 - b. Identifies period covered by the audit.
 - c. Identifies organizations & geographic locations where audit work conducted.
 - d. Cites the kinds/sources of evidence used, techniques, & methods of analysis.
 - e. Describes auditing standards applied or departures from standards.
 - f. Describes nature/extent of compliance testing.
 - g. Contains a statement on internal controls.
 - h. Indicates firm participating in the audit.
 - i. Indicates when exit conference held; with whom.

Yes No Note

3. Background (Optional) - Describes activity/entity audited & other info. to place issues in context.
4. Observations and Conclusions
- Responds to each audit objective.
 - Addresses all findings.
 - Relates findings to overall operations.
 - Addresses all major recommendations.
 - Identifies material instances of noncompliance with laws & regulations.
 - Indicates actions taken on prior audit reports.
 - Contains noteworthy accomplishments.
 - Discusses issues needing further study.
 - Privileged/confidential information noted.
 - Addresses weaknesses to be noted in yearend assurance memorandum.

PART II - FINDINGS AND RECOMMENDATIONS - all reports

1. Audit Finding:
- Neutral title.
 - Charge paragraph reasonable length and clear.
 - Contains criteria, condition, cause, and effect.
 - Consistent with details of finding.
2. Recommendations:
- Flow from the details in the finding, with a recommendation for each cause identified.
 - Address all actions needed to remedy cause(s).
 - Dynamic, reasonable, and specific.
 - Directed to lowest management level possible.
 - Unallowable/unreasonable costs addressed.
3. Management Reaction - Brief reaction to both the finding and recommendations.
4. Details of Finding:
- Sequence flows from charge paragraph.
 - Sufficient data to understand the finding.
 - Consistent with scope of work performed.
 - Each element completely developed.
 - Details clearly flow from one paragraph to next.
 - Captions "tonal" & assist in following finding.
 - Facts stated simply and in nontechnical language.
 - Examples used to explain problems described.
 - Visual aids used as appropriate.
 - Explains management's actions.
 - Opinions/conclusions reserved for concluding par.
 - Dollar savings report presented. Unallowable/unreasonable costs specifically addressed.

PART III - MANAGEMENT & AUDITOR COMMENTS - drafts & finals Yes No Note

1. Includes the following -
 - a. Concurrence or nonconcurrence in response to the finding & recommendation(s).
 - b. Recognizes corrective actions taken or planned.
 - c. Major points of contention presented.
 - d. Rebuttals based on facts rather than opinions.
2. Format includes the exact title of finding and -
 - a. Management comments
 - b. Auditor comments

GENERAL REPORT CHARACTERISTICS

1. Report written deductively.
2. Abbreviations/acronyms used correctly.
3. Appropriate capitalization.
4. Compound words correctly used.
5. Numbers spelled out/numeric characters used where appropriate.
6. Spelling is correct.
7. Report refers to position titles rather than names of individuals.
8. Report language is objective and noninflammatory.
9. Titles and headings are neutral, concise, and balanced.
10. Highlighting is reasonable, consistent, & appropriate.
11. Report is single-spaced.

OTHER COMMENTS/OBSERVATIONS:

REPORT REFERENCE SHEET

PROJECT CONTROL NUMBER:			PAGE: OF	
REPORT TITLE:			DATE OF REVIEW:	
REFERENCER:			AUDIT DIRECTOR:	
AUDITOR-IN-CHARGE:			AUDITOR:	
SYB.: (1)	PAGE NO.	PAR. NO.	LINE NO.	COMMENTS CLEARED

COMMENT OR SUGGESTED CHANGE: (Lines are optional) _____

DISPOSITION AND INITIALS: _____

SYB.: (2)	PAGE NO.	PAR. NO.	LINE NO.	COMMENTS CLEARED
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COMMENT OR SUGGESTED CHANGE: _____

DISPOSITION AND INITIALS: _____

SYB.: (3)	PAGE NO.	PAR. NO.	LINE NO.	COMMENTS CLEARED
-----------	----------	----------	----------	------------------

COMMENT OR SUGGESTED CHANGE: _____

DISPOSITION AND INITIALS: _____

REPORT REFERENCE SHEET

CONTINUATION SHEET			PAGE OF	
SYB.: (4)	PAGE NO.	PAR. NO.	LINE NO.	COMMENTS CLEARED

COMMENT OR SUGGESTED CHANGE:

DISPOSITION AND INITIALS:

SYB.: (5)	PAGE NO.	PAR. NO.	LINE NO.	COMMENTS CLEARED
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COMMENT OR SUGGESTED CHANGE:

DISPOSITION AND INITIALS:

SYB.: (6)	PAGE NO.	PAR. NO.	LINE NO.	COMMENTS CLEARED
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COMMENT OR SUGGESTED CHANGE:

DISPOSITION AND INITIALS:

SYB.: (7)	PAGE NO.	PAR. NO.	LINE NO.	COMMENTS CLEARED
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COMMENT OR SUGGESTED CHANGE:

DISPOSITION AND INITIALS:

EXAMPLE OF INDEXED AND REFERENCED DRAFT REPORT PAGE

① Authorization and Approval of Overtime

Conclusion Established overtime approval procedures were not followed and some
timekeeping units did not adequately plan work schedules in relations to leave
and other absences. As a result, overtime hours were not held to a minimum
and employees abused the use of overtime. Detail on the abuses of overtime
approval and authorization found during our review follow. Employees were
allowed or required to work excessive hours or to consistently work irregular
and occasional overtime year after year.

For example, a GM-15 earned \$10,864 in overtime pay in 1982, \$7,427 in
1983, and over \$3,000 in the first 12 pay periods of 1984. Another employee
at grade GS-08 was paid over \$12,000 for 818 overtime hours in the first 13
pay periods in 1984. Supervisors did not carefully plan work and schedule
leave and other absences. Employees took annual leave on the same day they
worked overtime, or on the days immediately prior to or subsequent to working
overtime. This practice was not consistent with DOE directives governing S
leave usage. Order 3630.1 which

Employees at grades GS-13 and above were allowed to choose whether they
would receive overtime pay or compensatory time, instead of being subject to a
mandatory requirement for GS-13's and above to receive compensatory time in
lieu of overtime. This practice is directly contrary
to DOE directives which contain

EXAMPLE OF COMPLETED REPORT REFERENCE SHEET

PROJECT CONTROL NUMBER:			PAGE 3 OF Many	
REPORT TITLE:			REVIEW DATE: 4/4/90	
REFERENCER: A. STICKLER			AUDIT DIRECTOR:	
AUDITOR-IN-CHARGE: D. REWRITE			AUDITOR:	
SYB.: (1)	PAGE NO. 1	PAR. NO. 1	LINE NO. 1	COMMENTS CLEARED <u>Yes</u>

COMMENT OR SUGGESTED CHANGE: Work cited in this section of draft report does not show evidence of supervisory review.

DISPOSITION AND INITIALS: Workpapers revised to show evidence of supervisory review. DR4/26/90 AS4/27/90

SYB.: (2)	PAGE NO. 1	PAR. NO. 2	LINE NO. 1-2	COMMENTS CLEARED <u>Yes</u>
-----------	------------	------------	--------------	-----------------------------

COMMENT OR SUGGESTED CHANGE: Your support consists of a workpaper summary which has not been traced to source and computations verified.

DISPOSITION AND INITIALS: Cited workpaper traced to source and computations verified. DR4/26/90 AS4/27/90

SYB.: (3)	PAGE NO. 1	PAR. NO. 2	LINE NO. 7	COMMENTS CLEARED <u>Yes</u>
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COMMENT OR SUGGESTED CHANGE: You cite "directives" (plural), but only show one directive governing leave usage for support.

DISPOSITION AND INITIALS: Sentence revised. DR4/26/90 AS4/27/90

SYB.: (4)	PAGE NO. 1	PAR. NO. 2	LINE NO. 2	COMMENTS CLEARED <u>Yes</u>
-----------	------------	------------	------------	-----------------------------

COMMENT OR SUGGESTED CHANGE: Need support that more than one DOE Directives contains a "mandatory" requirement re. GS-13 and above comp. time.

DISPOSITION AND INITIALS: Support added. Section A-3/4. DR4/26/90 AS4/27/90

SYB.:	PAGE NO.	PAR. NO.	LINE NO.	COMMENTS CLEARED ____
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COMMENT OR SUGGESTED CHANGE:

DISPOSITION AND INITIALS:

CHAPTER 13AUDIT RESOLUTION AND FOLLOW-UPA. SCOPE OF CHAPTER

The resolution and follow-up of audit recommendations is an integral part of auditing, and has a direct bearing on its effectiveness. Federal laws and regulations, OMB Circulars, and Departmental Orders provide for Departmental officials to establish and maintain a system to follow-up on the status of recommendations to ensure their implementation.

The IG is statutorily responsible for reporting to the Congress on progress made by the Department in implementing recommendations made in its reports. The IG Act Amendments of 1988 require the IG to prepare an annual report summarizing the activities of the Office during the previous year.

Audit resolution and follow-up encompasses those efforts taken by the Department, including the OIG, to address findings, implement accepted recommendations, and ensure follow-up necessary to verify completion of corrective actions. This chapter sets forth the policies and practices for audit resolution and follow-up with respect to implementation of OIG follow-up requirements that are the responsibility of AIGA.

B. RESPONSIBILITIES

The AIGA is responsible for audit follow-up in three important areas.

- o Review of Departmental position,
- o Review of corrective action indicated in the quarterly Departmental Audit Reports Tracking System (DARTS), and
- o Follow-up audits.

C. DEPARTMENTAL POSITION

The requirement for a Departmental position is established in DOE Order 2320.2B. Transmittals of final audit reports containing recommendations should remind the responsible Departmental Element that they should prepare a proposed Departmental position within 70 calendar days of the transmittal of the report. This proposed Departmental position will be reviewed by the Chief Financial Officer and submitted to the Secretary or a designee for approval. This Order also requires that within 15 calendar days after receipt of the approved Departmental position on a final audit report, the IG review the Departmental position and inform the Department Official responsible for audit resolution of any significant disagreement.

DOE Order 2300.1B, "Audit Resolution and Followup," dated 6-8-92, provides that any unresolved disagreement will be resolved by the Departmental Internal Control and Audit Review Council (DICARC).

1. AO Coordination. Within the OIG, the AIGA has primary responsibility for reviewing the Departmental position on audit reports. In discharging this responsibility AO is designated to coordinate the review with the responsible Assistant Regional Manager.

2. Regional Office Review. The responsible Assistant Regional Manager shall review the Departmental position and prepare comments thereon within the designated time established by AO, normally three days. The comments should indicate concurrence or nonconcurrence with the Departmental position. In the event of nonconcurrence, appropriate explanation shall be provided.

3. Reaching Agreement. AO shall review and discuss the response with the responsible Assistant Regional Manager, as required, in order to resolve any differences of opinion. Upon reaching an agreement, AO shall prepare a response for the AIGA which is to be signed by the IG. When a satisfactory agreement cannot be reached between AO and the Assistant Regional Manager, the matter will be referred to the AIGA for resolution. A copy of the Departmental position and related correspondence should be maintained in the workpapers. A copy should also be forwarded to AP3 so that the IGDBMS can be updated.

D. REVIEW OF CORRECTIVE ACTION REPORTED IN DARTS QUARTERLY REPORTS

DOE Order 2300.1B established a formal review system for audit follow-up by authorizing the DARTS. The Order requires the IG to review the DARTS status report submitted quarterly by Departmental Elements on IG audit reports and to notify the Chief Financial Officer of concerns or disagreements with the status of corrective action taken or planned. Significant unresolved disagreements on corrective action should be addressed by the DICARC.

The quarterly review is coordinated by AO for the AIGA. Upon receipt of the quarterly report by AO the responsible regions are provided information on the status of audit resolution for audits under their respective cognizance. Each region should review the status, including the completed or proposed action, and provide comments to AO. At this time, there is no requirement to ascertain that the completed action reported has actually occurred or that the completed action actually corrected the reported deficiency. Follow up review of corrective action will occur at a later time as subsequently discussed.

AO shall review and discuss the proposed comments with the responsible region as required and resolve any differences of opinion. Upon reaching an agreement, AO shall prepare a response for signature by the AIGA. When a satisfactory agreement cannot be reached between AO and the regional office, the matter will be referred to the AIGA for resolution.

E. FOLLOW-UP AUDITS

The Yellow Book requires auditors to follow-up on findings and recommendations from previous audits having an effect on audit objectives to determine whether prompt and appropriate corrective actions were taken by responsible officials. The standards state that:

Management is primarily responsible for directing action and following up on recommendations. However, auditors, in subsequent audits, should disclose the status of recommendations included in prior reports.

To implement our responsibilities we shall follow-up on recommendations contained in prior reports (IG or other) when subsequent audits are performed of a particular program, function or activity. However, in those matters of a critical/sensitive nature, a separate follow-up audit may be performed. If a follow-up audit of more than 10 days duration is scheduled, AIGA approval shall be required and an Planned Audit Profile shall be properly completed. Justification for performing the follow-up audit shall be adequately documented and maintained in the workpaper file.

DOE Orders and OMB Circulars also require that the IG perform periodic reviews of the Department's follow-up system to evaluate whether the system is adequate and results in timely and proper resolution of findings and recommendations. CRO is responsible for periodically performing this review.

CHAPTER 14GENERAL CONTRACT AUDITING POLICIES AND PLANNING**A. SCOPE OF CHAPTER**

This chapter introduces section IV of the Audit Manual, dealing with contract auditing. Contract auditing policies, a discussion of the different types of contract audits, and general guidance for contract audit planning and reporting are presented.

B. BACKGROUND

The contract auditor serves as a financial advisor to the contracting officer in the procurement process. Preaward audits provide the contracting officer with recommendations concerning the prospective contractor's cost proposal for negotiating an equitable contract price. Incurred cost audits furnish the contracting officer with recommendations concerning the acceptability of the actual costs claimed by the contractor. Because the auditors are independent of the procurement organization, they are able to offer objective recommendations to the procurement team. The contract auditor is able to advise the contracting officer on protecting the Government's interest by

- o evaluating the acceptability of costs proposed or claimed;
- o recommending new or revised contract clauses, including special cost provisions, (e.g., a ceiling on indirect cost rates);
- o pointing out potential accounting system weaknesses;
- o evaluating the financial capability of the contractor; and
- o pointing out any potential problem areas that could affect contract performance or cost.

To accomplish its mission, DOE enters into negotiated contracts with commercial organizations, non-profit organizations, and colleges and universities. These contracts range from firm fixed-price procurements, under which, for a set price, the contractor assumes full responsibility for all costs and resultant profits or losses, to cost-plusfixed-fee procurements, under which the contractor is reimbursed for actual costs plus a fixed profit amount. The term "contract auditing" refers to the review and evaluation of all costs proposed and incurred by contractor organizations completing the contract requirements.

1. Definitions. Terms frequently used in connection with contract auditing are defined in exhibit A (A:AM14EXA.WPF).

2. Timing of Contract Audits. A contract audit is performed at various times. The first review is performed by the auditor prior to the Department's entering into a negotiated contract. This preaward audit evaluates the

contractor's cost proposal, which estimates the costs to be incurred under a contract. Where there is no prior audit experience, a review of the prospective contractor's cost accounting system, indirect costing structure, and financial capability may also be required during the preaward audit. The contracting officer uses the audit results to negotiate the contract amount.

After a cost-type contract has been awarded, incurred cost audits are generally made as requested by the contracting officer or as scheduled by the cognizant audit office. When performing a cost incurred audit, the contract auditor reviews the costs claimed by the contractor to determine whether they are allowable under the terms of the contract and applicable laws and regulations.

A contract audit may also be made prior to settling a contract termination. The results of this audit are used in negotiating the contract termination settlement.

Except for small purchases--as defined in Part 13 of the Federal Acquisition Regulations (FAR), acquisition regulations and the contract terms require that for cost reimbursement contracts the amount of costs to be reimbursed to a contractor will be determined on the basis of an audit. In most cases, before the final amount of actual costs under a contract can be established and the contract closed out, the contracting officer will request a cost audit. On large contracts extending over more than one year, the contracting officer may request annual interim audits. Also, interim audits may be requested for smaller contracts extending more than one year when there are concerns such as the propriety of the cost being billed under the contract.

3. Relationship to DCAA Contract Audit Manual. Extensive use was made of the contract audit guidance contained in the DCAA Contract Audit Manual in developing this section of the Manual. The DCAA has developed detailed, professional guidance for each type of contract audit. The DCAA Contract Audit Manual is an excellent audit tool for employing advanced audit techniques and for special situations where more in-depth audit guidance is required.

4. Federal Acquisition Regulations. Throughout this section of the manual, reference is made to specific provisions in the FAR. Also, DOE Acquisition Regulations (DEAR) may in some cases modify the FAR. However, the contract provisions and the procurement regulations cited in the contract being audited will govern.

5. Relationship to Other Parts of the Audit Manual. Auditors involved in contract audits are responsible for understanding and implementing, where appropriate, policies and procedures discussed in Parts I, II, and III of this Manual.

C. AUDIT STANDARDS

The Yellow Book defines contract audits as "financial related" audits, requiring adherence to applicable AICPA SAs. Auditors must, of course, exercise their professional judgment in determining which standards apply to a given contract audit and which do not. The controlling consideration will be,

as with all audits, the specific audit objective or objectives. The auditor's determination that certain standards do not apply to the audit should be documented in the workpapers.

D. CONTRACT AUDIT COMPLETION TIME FRAME

Contract audits result from requests by contracting officers or their representatives. Some are very time-sensitive, requiring the auditor to schedule conflicting requests by assigning priorities. The following priorities have been established for the different types of contract audits:

1. Preaward Audit. Since the contracting officer needs the preaward audit to negotiate and award the contract, the auditor must give first priority to completing this audit and furnishing the results to the contracting officer by the date requested. OA's policy is to provide the contracting officer with written audit results within 45 days of the receipt of the request. The contracting officer should be advised verbally of the audit results as soon as they are available.

2. Closeout Audit. OA's policy is to provide the results of a closeout audit to the contracting officer within 120 days of the request, including all final closeout documents from the contractor.

3. Progress Payment/Contract Termination/Defective Pricing/Letter of Credit/Accounting System Audits/Financial Capability. These audits generally have requested completion dates and are thus handled similarly to preaward audits. The results should generally be provided within 45 days of the request. However, should a conflict arise between completing one of these audits and a preaward audit, the preaward audit is normally given priority.

4. Interim Cost Incurred Audit. For multi-year contracts, interim audits of incurred direct costs may be required. The frequency of interim audits will depend upon contract value and period of performance, or concern of the contracting officer (e.g., propriety of costs being billed under the contract). An interim audit of indirect costs may be required annually in order to finalize indirect cost rates. Results should generally be provided within 120 days of the request.

E. SMALL DOLLAR AUDIT

Generally, all cost reimbursable contracts are subject to audit. Contracting officers may, however, waive audits of small dollar value contracts. Audit requirements regarding dollar thresholds of contractor proposals are stated in FAR 15.805-5. DEAR 942.70 and FAR 42.7 provide guidance concerning dollar thresholds for incurred cost and indirect cost rate audits, respectively.

A full audit of a small dollar contract may be required even though not mandated by DOE regulations if the contracting officer's audit request results from current or prior problems with the contractor. However, if no problems have been experienced with the contractor, the audit scope of a small dollar contract may be limited to a desk review of such documents as the contract file, prior audit results, and indirect rates. Normally, desk reviews are not performed with OA resources, but are performed by an element of the

contracting organization. When performed by IG resources, the scope limitations should be documented in the audit workpapers and clearly stated in the audit report.

F. ENVIRONMENTAL RESTORATION MANAGEMENT CONTRACTORS AUDIT COGNIZANCE

Environmental Restoration Management Contractors (ERMCs) are responsible for managing the environmental restoration of sites separate from the existing management and operating contractor. The ERMCs generally are responsible for focusing solely on the environmental restoration of the site and subcontract all but the management and oversight of the cleanup. As of October 1993, the Department had ERMCs for the cleanup of two sites—the Fernald Restoration Site and the Hanford Restoration Site.

The DOE OIG is responsible for direct and indirect cost audits related to the Fernald site ERMC activity. DCAA is the cognizant audit agency for direct and indirect cost audits related to the Hanford site ERMC activity.

The difference in policy between the Fernald and Hanford sites is based on the contracting approach at these sites. At Fernald, the entire site is managed by one prime ERMC contractor, while the Department intends to retain as many as three M&O contractors in addition to an ERMC contractor at Hanford. These contractors will share management responsibilities of the Hanford facility.

G. WORKPAPER INDEXING SYSTEM

Workpapers must be prepared for all contract audit work in accordance with chapter 7 of this Manual. Because contract audits follow a relatively standard format, use of the following uniform indexing system is recommended.

<u>Section</u>	<u>Title and Content</u>
A	Administrative files (audit program, entrance conference letter, draft report, etc.)
B	Summary of Findings
C	Direct Labor
D/E	Fringe Benefits and Overhead Applicable to Labor
F	Material
G	Subcontract
H/J/K	Other Direct Costs
L	Overhead
M	General and Administrative Expense
N	Profit/Fee/Cost Sharing/Incentive Fee

H. CONDUCTING THE CONTRACT AUDIT

When conducting contract audits, auditors are required to follow established procedures, use the utmost care in identifying and marking proprietary data, maintain a relationship with OA (applies to auditors under contract), plan a visit to the contractor, develop finding attributes, and hold exit conferences at the conclusion of the audit.

1. General Procedures. Except as otherwise indicated below, auditors are generally required to conduct the contract audit in accordance with the guidance found in chapter 6 of this Manual. Chapters 15 through 19 provide suggested audit steps tailored specifically toward various contract audits.

2. Proprietary Data. When performing contract audits, consideration must be given to protecting proprietary data. The auditor keeps this information confidential and does not release it publicly. Under 18 U.S. Code 1905, the auditor can be held liable for disclosing proprietary data. Therefore, the auditor must use the utmost care in identifying and marking all such data in the workpapers. A notice, addressing the restrictions on releasing the information in the audit report, must be included on the title page of each report. If a subcontract is audited, a statement disclosing the subcontractor's views regarding release of the report to the prime contractor or a higher tier subcontractor should also be inserted.

3. Relationship of OA to Auditors Under Contract. Auditors under contract will, from time to time, perform contract audits. However, OA is responsible for overall quality and accuracy. OA will authorize the assignments, establish the audit objectives and scopes, and provide guidance prior to and during the reviews. OA will also be represented at the negotiation conference, if the auditor under contract is requested to attend.

4. Planning Visit. Normally, financial audits (including contract audits), do not require a survey similar to that used in a performance audit. However, in order to develop an effective audit program prior to the start of the field work, a planning visit may be needed, particularly if we have done no prior audit of the contractor. The purpose of a planning visit is to obtain data essential to planning the audit, including developing the initial testing plan. Information about the following are frequently obtained during such visits.

- o Contracts to be audited, including their nature, size, and cost principles;
- o Accounting systems; and
- o Internal controls.

A planning visit normally occurs after the audit has been approved but before the entrance conference and start of the field work. Planning visits are not required, but should be considered where feasible.

5. Finding Attributes. The extent of development of finding attributes in contract audits vary from situation to situation. Certain

attributes--criteria, condition, and effect--are always needed. Frequently, the recommendation is either explicit or implied with respect to questioned cost (i.e., recover the amount questioned). With respect to determining the cause, consideration should be given to such factors as the extent of effort required, the nature and significance of the finding, and contract size. When it is determined that the cause should not be developed, the recommendations should address the condition and related effect. When the cause is not developed, the reason therefore should be documented in the workpapers.

6. Exit Conference. Since there is normally no formal staffing of contract audit reports, the exit conference is held at the conclusion of the field work. The findings are discussed in detail (except only the facts related to questioned or unsupported proposal costs), and management comments/reactions are obtained verbally for inclusion in the audit report. An exit conference is not required for preaward audits.

I. REPORTING

As with performance audits, auditors are required to issue written reports according to Yellow Book standards.

1. General Policy. Auditors are required to follow the reporting policies established by the Yellow Book for financial and financial related audits. The Yellow Book requires written reports pursuant to the SAs to the extent they are relevant. In addition, the Yellow Book contains supplemental reporting standards.

a. Standards Similar to Performance Audits - In addition to the information provided in chapters 9 through 13 of this Manual, the following Yellow Book standards are applicable to contract audits and are essentially the same as for performance audits:

- o Statement on auditing standards used in the audit;
- o Reporting of illegal acts;
- o Omission of important information; and
- o Submission of written audit reports to responsible officials and the public.

b. Standards Dissimilar to Performance Audits - Two Yellow Book standards applicable to contract audits are somewhat different from their parallel performance audit standards. They are:

- o Report on compliance with laws and regulations (including positive and negative assurance), and
- o Report on internal controls.

Refer to the Yellow Book for specific guidance on these standards.

c. Guidance for Specific Contract Audit Types - Additional reporting guidance is provided below and in chapters 15 through 19 for specific types of contract audits.

2. Multiple Contract Audits. If an audit covers more than one contract, two or more reports may be required. Under normal circumstances, only one report is required for indirect cost audits. For interim and final audits on incurred costs, however, the number of reports will depend on the number of Government Departments or Agencies that have issued active contracts to the contractor. If different Government Departments or agencies are involved, separate reports for each Department or Agency are normally required.

3. Report Format. The final audit results are contained in a written report to the contracting officer. Because of time constraints, the results of preaward audits are frequently provided verbally to the contracting officer and later followed by a written report. The report should classify, by cost element, questioned costs (excluding unsupported costs on cost incurred audits), unsupported costs (preaward audits only), and unresolved costs. The bases for the costs so classified should be explained in the audit report. If direct costs are so classified, the auditor must determine if any indirect costs are allocable and state the appropriate amount.

Because contract audit results tend to be somewhat standardized, pro forma report formats have been developed. In addition to the information provided below, examples of the appropriate report format for each type of contract audit are included in chapters 15 through 19.

a. Report Cover - Contract audits will normally have a cover similar to that for Blue and Buff Cover reports, but printed on green paper. An example is provided in exhibit B (A:AM14EXB.WPF).

b. Title Page - An example of the title page for contract audit reports is provided in exhibit C (A:AM14EXC.WPF). It is important that the title page contain any restrictions on release of the report.

c. Table of Contents - An example of the table of contents for contract audit reports is provided in exhibit D (A:AM14EXD.WPF).

d. Body of Report - Examples of report formats are provided in other chapters for each type of contract audit report. However, basic elements to be included in reports are described below.

(1) Purpose and Scope. All reports should have a section which defines the audit scope and objectives. Information should also be provided on which cost principles govern in determining allowable costs.

(2) Circumstances Affecting the Audit. As necessary, reports should identify any scope limitations, restrictions on access to information, or other factors affecting the audit.

(3) Background. If necessary, background information needed to understand issues discussed in the report may be provided.

(4) Audit Results. This section of each report should summarize the auditor's review and evaluation of all costs proposed or incurred by the contractor organization. It should also contain language highlighting any findings in which questioned contractor costs are identified. Exhibit E (A:AM14EXE.WPF) provides suggested report language for costs considered unreasonable or expressly unallowable under contract terms.

(5) Other Matters to be Reported. As necessary, reports may include a section for matters not directly related to the audit objective, but which need to be included as a matter of record.

(6) Recommendations. Normally, recommendations in contract audit reports will be directed to the DOE contracting officer. If the audit identifies issues which necessitate recommendations to the field offices or to headquarters, the requirements for Blue or Buff Cover reports may apply.

(7) Offeror's or Contractor's Comments. This section of the report should briefly describe the contractor's comments (or offeror for preaward audits) on the audit results and recommendations.

e. Exhibits or Schedules - Material necessary to support data in the body of the report, such as supporting schedules, should be included with the report, as necessary. Exhibits or schedules are often illustrated as part of the report formats provided for the differing types of contract audit reports (see chapters 15 through 19).

4. Report Staffing. Because of the nature of many contract audit findings, and in order to expedite report issuance, the requestor is not provided with a draft version of the report prior to issuance. However, discussion of certain aspects of the findings with management is required. For preaward audits, the facts related to questioned or unsupported proposed cost are discussed with management to assure correctness. The report should indicate that the discussion occurred and identify the auditee officials. For all audit reports except preaward, all aspects of the findings are normally discussed with auditee management officials, such as facts, conclusions, and recommendations. Management's verbal reactions are included in the report.

J. FACTORS INFLUENCING CONTRACT AUDIT PLANNING

A number of factors must be considered in contract audit planning. These factors include:

1. Prior Audit Experience. Favorable prior audit experience with the contractor can reduce testing. For example, if prior audits of the contractor's proposals or claims uncovered only minor deficiencies, the auditor may consider reducing the audit testing. Unfavorable prior experience with the contractor, however, should suggest that the proposal or claim must be examined more extensively. Reviews by an effective internal audit staff can also influence the audit plan. In the final analysis, the auditor is responsible for the audit results, even if reliance is placed on other groups' audit experiences. A well-developed permanent file will provide the auditor with data on prior audit experience.

2. Type of Contract. The type of audit being conducted (preaward versus historical cost) and the nature of the contract(s) involved also influence the audit plan. For example, a preaward audit of a proposal for a cost-reimbursable contract will generally not require the same in-depth review as a proposal for a firm fixed price contract. Since the contractor will be reimbursed actual costs to be verified by subsequent audits, the amount of cost negotiated in the award process affects only the estimated fee. On the other hand, a firm fixed price contract is not subject to later audits (except for defective pricing purposes under Public Law 87- 653). Consequently, the contractor will enjoy any overstatement of costs that passes undetected during the preaward review as windfall profits. When developing the audit plan for costs incurred under cost reimbursable contracts, the auditor must bear in mind that such contracts do not offer management an incentive to control costs. Hence, the audit process may encompass a review of established controls to minimize costs as well as an audit of the costs for allowability.

3. Mix of Contract Types. If the contractor has a mix of cost reimbursable and fixed price type contracts, the audit plan should be sufficient to assure that management controls are in place to minimize the possibility of shifting costs from fixed price contracts to cost reimbursable contracts.

4. Extent of Government Business. If the contractor has a relatively small amount of Government business compared to commercial work, management controls established to enhance the commercial profits may be relied on to control costs, particularly if the Government work is similar to the commercial work. When Government business predominates, however, this assurance does not exist. Functional/operations audits directed towards reviewing management controls over decisions affecting economy and efficiency of operations would then need to be considered as well as a thorough review of the accounting and internal control systems. Reviews of proposed forward pricing indirect expense rates are also common at contractors with significant Government business. These reviews culminate in negotiating indirect expense rates used in bid proposals and involve a thorough analysis of contractor budgets. If the extent of the Government business is large, comprehensive audits of each cost element are separately accomplished as opposed to a single audit assignment encompassing costs charged to one or very few contracts.

5. Similarity of Effort to Commercial Business. If the proposed or contracted effort is similar to the contractor's commercial work, some degree of reliance may be placed on the controls established to enhance profit on commercial work. However, the audit plan must still be sufficient to assure that costs on the Government work are treated consistently with costs on commercial work, that the costs are properly identified by the cost accounting system, and that costs prohibited by Government regulations, or law, are not charged to the contract(s). Should the Government work be dissimilar to the contractor's commercial work, the extent of audit should be sufficient to determine if direct and indirect costs are treated consistently and if indirect costs are properly allocated to final cost objectives.

6. Reliability and Integrity of Accounting System. The reliability and integrity of the contractor's accounting system can affect the audit plan. For example, larger contractors tend to have more elaborate cost accounting and more reliable internal control systems than small contractors. A

well-designed cost accounting system surrounded by a good system of internal controls can reduce the testing, particularly if there has been good prior experience with the contractor. However, the auditor will probably need to increase testing when encountering a deficient cost accounting system or a system with weak internal controls.

7. Special Audit Requests. In setting the audit scope, the auditor must consider any special requests of the contracting officer. Such requests can either increase or decrease the audit scope. Special audit requests should be clearly discussed in the scope section of the audit report and detailed audit steps should be designed for their accomplishment.

K. GENERAL CONTRACT AUDIT PROGRAM

Auditors should familiarize themselves with the generalized audit plan included in chapter 17 of this Manual. Additional general audit steps applicable to contract audits include the following items. More specific audit steps, related to each type of audit, are presented in chapters 15 through 19.

1. Review the permanent file to determine prior audit experience with the contractor, whether approved forward pricing rates exist, the extent of reliance that can be placed on the contractor's accounting and internal control systems, mix of contracts, extent of Government business, etc.
2. Determine the status of recommendations from prior audits. Consider the impact of the status (open/cleared), and the date the actions occurred, on the current audit.
3. Review the audit request from the contracting officer and/or the AIGA to determine when the audit results are required and whether there are any special audit requests, such as accounting system reviews.
4. Review the contract to ascertain whether the contract terms or special provisions will affect the audit scope or extent of compliance testing. The contract should reference the governing procurement regulations and disclose whether any specific regulations are exempted and whether the Cost Accounting Standards (CAS) apply.
5. Review the applicable internal controls. Consider the potential for fraud, waste, and abuse. Identify weaknesses and assess control risk.
6. Prepare a detailed audit program based on the above determinations and consider the factors affecting the audit planning noted in this chapter.

DEFINITIONS OF CONTRACT AUDIT TERMS

1. Accounting System Review. A review of a contractor's accounting system and system of internal controls to evaluate whether they are adequate to segregate, accumulate, and report actual contract costs. (See chapter 21.) This review is frequently requested and performed in conjunction with a preaward audit.

2. Contract Audit. For the purpose of this section of the manual, a contract audit includes any of the following:

- o Preaward audit;
- o Cost incurred audit;
- o Indirect cost audit;
- o Accounting system review;
- o Financial capability;
- o Contract termination audit;
- o Defective pricing audit;
- o Letter of Credit audit;
- o Progress payment review; and
- o Verbal verification of rates (labor, overhead, etc.)

3. Contract Termination Audit. An audit conducted upon complete or partial termination of a contract for the Government's convenience, to evaluate the costs (and related fee or profit, if any) for which the contractor has claimed reimbursement. (See chapter 19.)

4. Cost Accounting Standards. Promulgated by the former CAS Board (CASB) under Public Law 91-379 to achieve uniformity and consistency in the cost principles and cost accounting practices followed by Government contractors and subcontractors.

5. Cost Incurred Audit. An interim or final audit conducted to evaluate the allowability of direct costs claimed on a cost type contract. This audit may also encompass an audit of indirect costs. (See chapter 16.)

6. Cost Plus Award Fee Contract. A cost-reimbursable contract that provides for a fee consisting of (1) a base amount (which may be zero) fixed at inception of the contract and (2) an award amount, based upon a judgmental evaluation by the Government, sufficient to motivate excellence in contract performance.

7. Cost Plus Fixed Fee Contract. A cost-reimbursable contract that provides for paying the contractor a negotiated fee that is fixed at the inception of the contract.

8. Cost Plus Incentive Fee Contract. A cost-reimbursable contract that provides for an initially negotiated fee to be adjusted later by a formula based on the relationship of total allowable costs to total target costs.

9. Cost Sharing Contract. A cost-reimbursable contract in which the contractor receives no fee and is reimbursed only for an agreed upon portion of its allowable costs.

10. Cost-reimbursable Contract. A contract which provides for contractor reimbursement based on actual, allowable costs incurred up to a specified ceiling amount. The contract may or may not call for the contractor to receive a fee.

11. Defective Pricing Audit. An audit conducted after award pursuant to the Truth in Negotiations Act (Public Law 87-653) to determine if costs proposed by a contractor and accepted by the Government were current, complete, and accurate when agreement was reached on the contract price. (See chapter 19.)

12. Direct Costs. Costs clearly identifiable as being incurred specifically for contract efforts. Direct costs normally include labor, materials, subcontracts, travel, etc.

13. Federal Acquisition Regulation (FAR). The Government-wide procurement regulations applicable to both civil departments and Agencies and Department of Defense Agencies on and after April 1, 1984.

14. Financial Capability. An evaluation of a prospective contractor's cost flow projections and underlying assumptions and an assessment as to whether the projected cash flow is sufficient to meet all financial requirements during the proposed contract period, taking into consideration the method and timing of payment contemplated. This review is frequently requested and performed in conjunction with a preaward audit. (See chapter 19.)

15. Firm Fixed Price Contract. A contract that provides for a price that is not subject to any adjustment based on the contractor's cost experience in performing the contract. This contract type places maximum risk for controlling costs and resulting profit or loss on the contractor.

16. Fixed Price Contract With Economic Price Adjustment. A contract that provides for upward and downward revision of the stated contract price based upon the occurrence of specified contingencies. The most commonly used price adjustments are: (1) adjustments based on changes in published or otherwise established prices of basic commodities and commercial items and (2) adjustments based on substantial variations from anticipated changes in a selected labor or material cost index, e.g., Bureau of Labor Statistics indices.

17. Fixed Price Contract With Prospective Price Redetermination. A fixed price contract that provides for a firm price for an initial period of performance and, after that, prospective redetermination of the price for a subsequent period of performance.

18. Fixed Price Incentive Contract. A fixed price contract that provides for adjusting profit and establishing the final contract price by a formula based on the relationship of final negotiated cost to the target cost.

19. Forward Pricing Agreement. An agreement entered into by a Government contracting authority and a contractor establishing forward pricing rates, such as for labor, overhead, general and administrative expenses, etc., to be used for a specified period of time in preparing contract pricing proposals.

20. Generally Accepted Government Auditing Standards (GAGAS). General, field work, and reporting standards for financial and performance audits as stated in *Government Auditing Standards*, 1988 Revision, issued by the Comptroller General of the United States (commonly referred to as the "Yellow Book").

21. Generally Accepted Accounting Principles (GAAP). The rules and practices, both written and unwritten, which represent accepted accounting principles and practices as evidenced by substantial authoritative support.

22. Indirect Cost Audit. An audit of a contractor's indirect costs (overhead, general and administrative [G&A] expense, and other allocated expenses) conducted to establish final rates for a fiscal year or rates to be used for proposals or forward pricing rate agreements. (See chapter 17.)

23. Indirect Costs. Costs which benefit the contract but which are not incurred solely for the contract. Indirect costs normally consist of overhead, general and administrative, and other costs charged on an allocation basis.

24. Letter of Credit Audit. An audit conducted to establish whether a contractor's cash management and monitoring practices are adequate to ensure proper accounting for and physical security of funds drawn down and if cash balances are maintained at a minimum level needed to satisfy only immediate payment needs. (See chapter 19).

25. Preaward Audit. An audit conducted prior to the award of a contract to evaluate the allowability of the prospective contractor's proposed costs. The contracting officer uses the results of such audits during negotiations with the contractor to establish the contract price. Preaward audits are made for both cost reimbursable and fixed price contracts. (See chapter 15.)

26. Progress Payment Review. A review performed to determine whether progress payments claimed under a fixed price contract are in accordance with the contractor's progress payment provisions and applicable regulations.

27. Questioned Costs. Costs which are considered (1) unreasonable in nature or amount, (2) not allocable to Government work on the basis of benefits received, (3) not in compliance with CAS, or (4) expressly unallowable under the contract cost principles or other contract terms.

28. Statement on Auditing Standards (SAS). Statements issued by the Auditing Standards Board of the American Institute of Certified Public

Accountants that are recognized authority on generally accepted auditing standards.

29. Unresolved Costs. Costs on which a determination on allowability has not been made, because the auditor is waiting for an assist audit of a subcontractor or a contracting officer's decision on an outstanding item, such as benefits DOE derives from contractor's Independent Research and Development (IR&D) program.

30. Unsupported Costs. Proposed costs for which the offeror has not furnished adequate documentation or support. Unsupported incurred costs are clarified as questioned because they are unsupported.

31. Verbal Verification of Rates. Information on labor rates, overhead rates, general and administrative expense rates, etc., supplied to a procuring office in the absence of a preaward audit or formal audit report. (See chapter 19.)

EXAMPLE OF TITLE PAGE
CONTRACT AUDIT REPORT

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITS

TITLE OF AUDIT IN CAPITAL LETTERS
(MAY INCLUDE TYPE OF AUDIT,
CONTRACT NUMBER, NAME OF
CONTRACTOR, AND
CITY, STATE)

This audit report may contain proprietary or other sensitive information. The restrictions of 18 U.S. Code 1905 should be considered before this information is released to the public.

Under the provisions of Title 32, Code of Federal Regulations, Part 290.26(b)(2) (as amended August 10, 1977), all Freedom of Information Act requests for audit reports received by the OIG will be referred to the cognizant contracting officer for determination as to releasability and a direct response to the requestor. Furthermore, the information contained in this report should not be used for purposes other than those intended without prior consultation with the Department of Energy's Office of Inspector General regarding its applicability.

Report Number:
Date of Issue:

____ Regional Audit Office
City, State Zip
Prepared By: John Doe & Company

EXAMPLE OF TABLE OF CONTENTS
CONTRACT AUDIT REPORT

REPORT NUMBER:

TITLE OF AUDIT IN CAPITAL LETTERS
(MAY INCLUDE TYPE OF AUDIT,
CONTRACT NUMBER, NAME OF
CONTRACTOR, AND
CITY, STATE)TABLE OF CONTENTS

	<u>Page</u>
Purpose and Scope	x
Circumstances Affecting the Audit	x
Background (Only if needed)	x
Audit Results	x
Other Matters to Be Reported	x
Recommendation(s)	x
Contractor's (or Offeror's) Comments	x
Supporting Exhibits and Schedules (may be numbered as a continuation of report page numbers or each exhibit may be separately numbered--e.g., A-1, A-2; B-1, B-2, etc.)	

EXAMPLE OF AUDIT REPORT LANGUAGE
ON QUESTIONED COSTS

In accordance with the responsibilities set forth in DOE Order 2321.1, "Auditing of Programs and Operations," the OIG is required to conduct audits of the activities of the Department and its contractors and financial assistance recipients. These audits are classified as either financial or performance audits. In conducting these audits, auditors should follow the applicable standards included in the Yellow Book. This exhibit provides suggested audit report language to disclose questioned costs that are not in compliance with the contract. For example, a cost may be considered unreasonable or expressly unallowable under the contract terms.

All audit reports in which questioned contractor costs are identified should contain language highlighting such findings. The precise language will depend on the nature of the finding. We have identified four potential scenarios that require somewhat different audit report treatment.

A. EXPRESSLY UNALLOWABLE

We identified contractor costs that are expressly unallowable under the terms of the contract (specific contract provision). (An example would be a charitable contribution.)

1. Disclosure. The text of the report would include the following language:

Based on our review, we concluded that the contractor made a charitable contribution. A review of the terms of the contract showed that such charges are unallowable (cite terms of contract).

2. Recommendation. In the recommendations section:

We recommend that the contracting officer (or other appropriate official) take prompt action to recover the funds that were used by the contractor for a charitable contribution contrary to the terms of the contract. The contracting officer should also ensure that the contractor initiate necessary internal controls to assure that similar charges will not be incurred in the future.

B. UNREASONABLE COST(S)

We identified unreasonable costs which have been incurred without either the express or implied approval of the DOE.

1. Disclosure. The text of the report would include the following language:

The costs incurred by the contractor as identified in this report, in our opinion, represent unreasonable costs under the terms of this contract (cite contract provision).

2. Recommendation. In the recommendations section:

We recommend that the contracting officer recoup (state amount) questioned as being unreasonable and therefore unallowable. Also, the contracting officer should take necessary action to assure that the contractor is prohibited from incurring such costs in the future and to prevent future cost disallowances.

C. UNREASONABLE COST(S) APPROVED BY DOE

We identified contractor incurred costs which we believe are unreasonable and we therefore questioned these costs. However, a DOE official either directly or indirectly approved the incurred cost.

1. Disclosure. The text of the report would include the following language:

In our opinion, the costs identified in this report (for example, the costs of operating the facilities at the McCarran Airport by Los Alamos, Livermore and Sandia) are unreasonable. The contract with _____ (Provision 970. 5204-13) provides that costs must be reasonable in order to be considered allowable. Consequently, we question such cost. The contractor should be notified that future incurrence of such costs will be considered unreasonable and will be subject to disallowance under section _____ of the contract. The Office of Inspector General will review this area of contractor operations in the future and will evaluate whether appropriate action has been taken by the contracting officials.

2. Recommendation. In the recommendations section:

We recommend that the contracting officer (or appropriate equivalent) formally notify the contractor that in the future DOE will not reimburse the types of costs that have been found to be unreasonable in this audit report.

B. UNREASONABLE - INADEQUATE TECHNICAL JUDGMENT

We identified and questioned contractor costs that we believe are unreasonable and, thus, unallowable (whether or not expressly approved by a DOE official) because they resulted from inadequate technical judgment(s). An example would be the payment of laboratory test costs when the contractor had prior knowledge that generally accepted scientific protocol was not followed when the tests were performed.

1. Disclosure. The text of the report would include the following language:

In our opinion, the laboratory testing costs identified in the report are unreasonable since the contractor, under the terms of the contract, was expected to exert expert technical (scientific) judgment in carrying out the mission assigned by DOE.

2. Recommendation. In the recommendations section:

We recommend that the contracting officer recoup from the contractor the questioned funds identified in the report as being unreasonable and unallowable. Also, the Department should take prompt action to prevent similar occurrences in the future.

CHAPTER 15PREAWARD AUDITSA. SCOPE OF CHAPTER

This chapter provides guidance for audits of cost or pricing data submitted by an offeror in response to a request for a proposal which will result in a negotiated contract/subcontract or modification to an existing contract.

B. OBJECTIVE OF A PREAWARD AUDIT

The objectives of a preaward audit are to evaluate the allowability, allocability, and reasonableness of the offeror's proposed costs. The audit results will be used as a basis for negotiating a contract price.

C. BACKGROUND

The contracting officials' responsibility includes price and cost analyses of price proposals according to the contract cost principles, FAR and DEAR. Auditors performing contract cost audits should determine the applicability of CAS.

1. Responsibilities of Contracting Officials. DOE contracting officials are responsible for conducting price or cost analyses of price proposals for negotiated contracts and subcontracts. Both price and cost analyses help determine whether a proposed price is fair and reasonable for the work to be performed.

2. Application of Contract Cost Principles. The contract cost principles and FAR requirements, as supplemented by the DEAR, are to be used in determining allowable costs for pricing DOE contract and subcontract actions requiring cost analyses. When auditing contracts issued by other Departments/Agencies, the governing Departmental/Agency regulations should be used.

3. Application of Cost Accounting Standards. The auditor should determine the applicability of CAS at the start of the audit. Small business contractors are exempt under the CAS. However, whether the offeror is fully CAS covered or subject to only modified CAS coverage, certain standards apply. These standards are (1) Standard 401, Consistency in Estimating, Accumulating, and Reporting Costs, and (2) Standard 402, Consistency in Allocating Costs Incurred for the Same Purpose. Additionally, a number of standards have been incorporated in selected FAR cost principles. When auditing a particular cost item, the auditor should refer to the related cost principle to determine whether a cost accounting standard applies even though the contractor may not be subject to the standards. The major provisions of these standards are included in exhibit A (A:AM15EXA.WPF). Chapter 19 contains additional guidance for applying CAS during preaward audits.

D. NOTIFICATION TO AIGA REPRESENTATIVE OF UNUSUAL CIRCUMSTANCES

The auditor should report the following conditions, which may develop during an audit at the offeror's offices, to the DAIG/AO--through regional management--immediately in order to obtain a determination regarding the feasibility of continuing the audit.

- o Denied or restricted access to the offeror's books and records considered essential to the conduct of the audit.
- o Estimating deficiencies so great that the pricing proposal is seriously impaired as a basis for negotiation.
- o Suspicion of fraud or other illegal activity.

E. AUDIT APPROACH

A preaward audit of cost or pricing data is designed to evaluate

- o the propriety of the contractor's proposal, including the soundness of the estimating system and practices;
- o the reliability of source data provided;
- o the reasonableness of any judgmental factors;
- o the degree of compliance with established company and Government policies, procedures, and regulations; and
- o the dollar impact on the proposed costs of any deficiencies noted while performing the above evaluation.

F. INITIAL AUDIT STEPS

Preward audits include initial audit steps to review audit requests, verify computations, confer with requesters, and prepare acknowledgments.

1. Review Audit Request. Review the audit request and as many of the following documents as have been made available for completeness (some documents will only be available at the contractor's offices):

- o the contract solicitation or the actual contract draft, including the statement of work, period of performance, and special conditions;
- o the pricing proposal and accompanying cost or pricing data;
- o any special requests from contracting officials; and
- o the permanent audit file.

2. Verify Computations. Verify the computations and extensions of the pricing proposal.

3. Confer With Requester. Before undertaking the audit, confer with the requester regarding the following, where applicable, after the initial review of the above documents:

- o apparent incomplete or missing documentation;
- o necessary arrangements for technical analysis;
- o unclear matters; and
- o arrangements for audit of subcontracts and intracompany proposals.

4. Prepare Acknowledgment. Prepare an acknowledgment (if it has not already been prepared by the regional coordinator) of the request confirming the due date for transmitting the verbal and written reports and any other significant matters affecting the audit.

G. COST ACCOUNTING SYSTEM

Understanding the offeror's cost accounting system allows the auditor to identify deviating variables.

1. Importance of Cost Accounting System. Knowledge about an offeror's cost accounting system is important in any preaward audit. Variables which affect the effort devoted to reviewing a cost accounting system include: (1) whether the information on file is obsolete and (2) the dollar value of the current pricing proposal and its overall significance in terms of the firm's annual sales volume.

The review of a cost accounting system should disclose whether:

- o the breakdown of cost accounts is adequate for estimating and determining costs;
- o cost classifications are consistent;
- o double counting, which distorts results, is avoided; and
- o the auditee is employing cost accounting for cost control, thus helping to establish that costs are reasonable when the auditee may not be subject to competitive restraints.

If the dollar value of the pricing proposal being audited is significant in relationship to the auditee's total sales and if information about the auditee's cost accounting system is not current, the cost accounting system may have to be reviewed in conjunction with the preaward audit of cost or pricing data. If this review was not provided for in the audit scope, the auditor (whether IPA or OIG) will confer with the DAIG/AO before proceeding, since time restrictions may impact the amount of work. The auditor should describe the circumstances encountered and the effort necessary to gain assurance regarding the adequacy of the auditee's cost accounting system. A separate audit guide is available for reviewing a cost accounting system in chapter 19.

Cost accounting system documentation on file should be updated with any pertinent changes noted during the preaward audit.

2. Verification of Rates and Job Classifications. Average labor rates may be developed by job classification groupings, by department or cost center, or on a plant-wide basis. Rates developed on a job classification basis are generally preferable, because they provide homogenous groupings, and because group average rates are generally representative of the labor cost to be incurred. Rates developed on a plant-wide basis are generally unacceptable because of the wide fluctuations in pay rates normally found in a total plant concept.

a. Average Labor Rates - Labor rates developed on an average basis should be compared to current wage rates of employees included in the grouping to ascertain that the average rates are accurate and that the classifications included in the groupings are homogeneous and representative of the effort to be expended on the contract. Projected average rates may be higher or lower than experienced averages when the contractor's business is increasing or decreasing, as significant numbers of new hires or layoffs affect the averages. At large contractor locations, a forward pricing rate agreement may have been negotiated with contracting officials. Unless the auditor is aware of any circumstances leading to a belief that negotiated rates are no longer current, the proposed rates can be verified by comparing them to the agreement.

b. Individual Labor Rates - Individual rates may be used when the caliber of people used for certain research or scientific work does not represent average labor classification rates. In these cases, check the proposed labor rates of named individuals against personnel or payroll records to determine the reasonableness of the proposed rates.

c. Escalation of Labor Rates - As a general rule, wage or salary escalation factors are applied to current labor rates to project costs over the period of performance of the contract. Determine if escalation rates are in accordance with current planning, budgeting, and personnel policies and if the factors are not excessive when compared with general economic forecasts and wage agreements. Care must be exercised in insuring that escalation factors are properly applied to base wage rates to yield the average wage rates expected to be experienced on the contract. This can be illustrated as follows:

Assumptions:

- o The auditor is reviewing a proposal anticipating a period of performance from January 1, 1990 to December 31, 1990.
- o The estimated labor effort is expected to be level throughout 1990.
- o The contractor's policy is to grant wage increases on the employee's anniversary date rather than granting wage increases to all employees on the same date.
- o The expected escalation rate is six percent.

- o The base wage rates (prior to escalation) used by the contractor (latest available) were as of September 30, 1989.

Calculation of escalation factor:

- o Since the effort is expected to be level, the average wage rate would be that in effect at the midpoint of contract performance - June 30, 1990.
- o The span of time from the date of available base rates (September 30, 1989) to the midpoint of contract performance June 30, 1990) is nine months.
- o The escalation factor to be applied to the base rate would be 9/12ths of six percent, or 4.5 percent.

d. Compliance With Labor Laws - Where applicable, tests should be made to assure that wage rates meet the requirements of the Service Contract Act of 1965 and the Walsh-Healey Public Contracts Act and that overtime compensation conforms to the Contract Work Hours and Safety Standards Act. Applicability of these legislative acts will be apparent by their inclusion in the solicitation or draft contract.

e. New Job Classification - If the firm's policy manual does not include any of the proposed job classifications, determine contractor's justification for creating new classifications for the proposal and evaluate basis for developing the rates.

3. Justification for Direct Charge Classifications. Determine whether the proposed job classifications are consistently charged as direct labor. Also determine whether the type of labor called for is treated consistently as direct labor on other work.

4. Overtime Premium. Overtime premium is normally charged to contracts as "other direct costs" or included in overhead. If the contractor includes overtime premium as direct labor or "other direct costs," the practice should be consistently followed and carefully examined to assure that the Government cost type work is not singled out to be done on overtime.

5. Estimates Based on Historical Experience. When the direct labor hours and labor mix proposed are based on historical experience, determine if the data apply to the proposed effort and whether suitable adjustments have been made to consider nonrecurring costs and productivity improvements. Nonrecurring labor costs occur, for example, when previously fabricated components are to be purchased for the proposed contract. Productivity improves when tasks are performed repetitively. Appendix F of the DCAA Contract Audit Manual is useful in improvement curve analyses and evaluating the contractor's improvement curves.

6. Estimates Based on Standard Costs. Where direct labor estimates are based on standard costs, the auditor should be sure that the standards are updated periodically and that variances are properly applied. In this regard

the auditor should refer to CAS 407 - Use of Standard Costs for Direct Material and Direct Labor which provides criteria under which standards may be used for estimating and recording costs.

7. Estimates Based on Technical Data. Where the direct labor hour and labor mix are developed from technical information, such as engineering designs and specifications, technical analysis will likely be required to establish the estimates' reasonableness and completeness.

H. DIRECT COST ESTIMATES

The methods employed in developing cost estimates may vary significantly because of the peculiarities of the different types of work covered by the proposals. Attention should be placed on how cost elements are developed and integrated into the total estimates of direct material, subcontracts and other direct costs.

1. Direct Material. Direct material normally represents a substantial part of the total costs shown in proposals and therefore warrant the following:

a. Need for Technical Analysis - Technical analysis is generally needed to evaluate the kinds and quantities of proposed material.

b. Value of Graphic Analysis - Where material costs are significant, improvement curves may be appropriate for plotting vendors' prices and quantities for parts and components which are purchased repetitively. (Use DCAA Contract Audit Manual Appendix F or other reference outlining improvement curve analysis techniques.)

c. Examination of Underlying Data-Material Quantities - Where production yield factors are used in estimating material quantities, determine if the factors are supported by current experience and trend data and are adjusted for anticipated changes.

Where material quantities include allowances for process scrap, material spoilage or losses during fabrication or assembly, or inventory obsolescence, determine if the allowances are clearly identified, properly applied, and adequately supported.

If this is a follow-on procurement, ascertain whether residual Government-owned inventories have been factored into the bill of materials at no cost.

d. Examination of Make or Buy Decisions - Determine whether the offeror's decisions to make or buy major components and parts were based on pertinent factors, such as (1) relative costs, (2) available capacity, (3) subcontractor's capabilities, etc. A technical evaluation of the make or buy program may be appropriate. Assess whether make or buy cost comparisons are realistic and include appropriate loading factors and indirect costs.

e. Justification for Direct Classification - Determine if the bill of materials includes only those items which are consistently treated as

direct charges to contracts. Items used for the same purpose should not be charged as both direct and indirect costs.

Determine if the proposed accounting treatment of scrap conforms to the company's policy. Also, determine whether income from scrap sales is equitably credited to contract costs.

f. Verification of Material Costs - Compare proposed prices for direct materials to current vendor quotations. Evaluate the extent of price competition. Where price competition for significant material items is inadequate, examine the analysis made to establish reasonableness of price. If subcontractor cost or pricing data were audited, review the results of both the audit and the negotiations conducted to arrive at a final price. Generally, subcontracts will not be negotiated prior to award of the prime contract.

Compare the proposed prices with previous purchases (adjusted for quantity differences) of the same materials, whether or not they were used on Government work. Determine what consideration has been given to price reductions for (a) elimination of nonrecurring costs such as start-up or tooling costs, (b) changed market conditions, and (c) quantity discounts. If prices are based on standard costs, also determine whether the variance factor applied is realistic and current.

For items purchased at fixed prices from the company's own divisions, affiliates, or subsidiaries, assure that intercompany profit is not passed on to the Government unless authorized by FAR 31.205-26(e).

2. Subcontracts. If the proposal includes large subcontracts, determine whether the subcontract price was based on adequate price competition. If the procurements are sole or single source, ascertain whether the contractor or the contracting official has arranged to audit the proposed costs. Generally, the contracting official arranges for audits to be performed.

If the contractor has made any price analyses or preaward audits of subcontract proposals, the related workpapers should be examined to determine whether the review was adequately accomplished. Also determine whether the offeror's past negotiations with subcontractors consistently resulted in prices lower than were initially proposed. If so, appropriate comments should be included in the audit report.

3. Other Direct Costs. In general, the evaluation of methods and procedures for developing estimates of other direct costs should consider the following:

a. Justification for Direct Classification - All proposed costs related to items classified as "other direct" should be carefully reviewed to determine whether the classifications conform to company policy and are consistent with treatment of these items for other (commercial) work.

b. Use of Percentages or Conversion Factors - If any cost items are based on applying percentage or conversion factors to direct labor or direct materials, such factors should be compared to historical cost data. Special

tooling, field service, and packaging costs are sometimes estimated in this manner.

c. Miscellaneous Other Direct - Other direct charges will often include the following:

(1) Travel and Subsistence. Travel costs include costs of transportation, lodging, subsistence and incidental expenses, incurred by the offeror's personnel in a travel status while on official business.

(a) Determine whether proposed per diem amounts are in accord with the offeror's standard policy and whether the amounts are reasonable (See FAR 31.201-3). FAR 31.205-46 should be carefully reviewed since that cost principle establishes limitations on reimbursable per diem costs.

(b) Ascertain whether air transportation cost estimates are based on use of less than first class service (FAR 31.20546).

(c) To aid in judging whether the costs are reasonable, compare the proposed number of trips (and number of concurrent travelers) and lengths of stay with experience on similar work. Generally, the necessity for the number of trips is subject to technical evaluation.

(2) Computer Costs. Verify the data supporting proposed computer rates. Refer to chapter 16 for audit guidance in examining algorithms used for costing purposes. If indirect costs are included in the rate, assure that the costs are not duplicated in a general allocation elsewhere in the proposal. Verify that profit is excluded from the rate.

(3) Special Tooling. This category pertains to special tooling required to produce specific end items and excludes perishable type hand and machine tools or other multi-purpose equipment items.

(a) Where possible, compare estimates for special tooling with previous production, making appropriate adjustments. Adjustments may be necessary to reflect differences in complexity of the product or improvements in methods and techniques. In complex situations, technical assistance may be needed. Ascertain whether tooling from prior or concurrent contracts is available for use without charge.

(b) Assure that the list of tooling reflects what the Government will furnish (where applicable) and that it excludes replacement and maintenance-type tools, which are recorded as indirect costs, and items of a capital nature.

(c) If the pricing proposal is for a follow-on production order or for spare parts, the tooling list should not include costs for basic tooling requirements already charged to the end items of the first production contract, except when replacements are required.

(d) Guidelines for auditing direct material estimates can generally be applied to purchased tooling.

(4) Packaging. Compare proposed costs with costs incurred on other work for similar types and kinds of packaging.

I. INDIRECT COST ESTIMATES

Indirect cost estimates are generally prepared for an ensuing period by projecting the amount of each expense in the overhead category and its allocation base. The projections should normally be made by reference to the following:

1. Previous Audit Experience. If incurred indirect costs allocated to active cost-type contracts or subcontracts have been audited, these audit results may be useful in evaluating indirect cost rates in connection with a preaward audit, particularly where the rates are based on historical costs. However, when using historical data the auditor must establish that the history fairly represents expected experience during the proposed period of contract performance. Major cost accounting changes since the last audit should be identified. The audit of incurred costs would have established

- o the composition of indirect cost pools;
- o the allowability of indirect costs to be allocated to Government work;
- o the consistency in classification of indirect costs;
- o the equitability of the allocation bases used;
- o the appropriateness of the accounting period for allocation of indirect costs; and
- o the overall reliability of the indirect cost allocation system and the reasonableness of the final result of the indirect cost allocation process.

Where indirect cost estimates are based on historical costs, evaluate the propriety and impact of any proposed or actual changes in the accounting treatment of costs or allocation process.

To evaluate proposed indirect cost rates further, compare the data presented with approved company budgets for the proposed period. Compare trends in the proposed rates with the prior year and with current experience. Evaluate the impact of any nonrecurring events (such as plant rearrangements or expiration of rental agreements) as well as the effect that the contract to be awarded has on the experienced rates. Ascertain if evidence of excess or idle facilities exists in the contractor's plant. If so, the costs of such facilities may be questioned (See FAR 31.205-17).

Where forward pricing indirect expense rates have been negotiated with the contractor covering the period of proposed contract performance, the negotiated rates should be accepted unless the assumptions upon which the rates were negotiated have changed. As an example, if award of the proposed contract materially affects the production volume, the rates will be significantly reduced.

2. No Previous Audit Made. If no previous audit has been made of incurred indirect costs, it is necessary to examine the costs comprising the indirect expense pools and the equitability of the allocation bases. Chapters 17 and 18 of this Manual include guidance that can be applied in evaluating proposed indirect cost pools and allocation bases.

Review the composition of indirect cost pools for proper classification of costs and suitable segregation by category and by characteristics (i.e., variable, semi-variable, and non-variable). Where a significant change (either up or down) in volume from the prior period is contemplated, ascertain whether variable or semi-variable indirect costs show a corresponding change. Review indirect costs of a non-variable nature which show significant variations between historical cost and proposed estimated cost.

Ascertain whether expressly unallowable costs are excluded from the indirect cost pools and, where appropriate, are included in the allocation base. Assure that allocated indirect cost pools do not include costs recovered through application of loading factors to another cost base, e.g., material handling rate.

3. Payroll Taxes and Fringe Benefit Costs. Verify that Federal Insurance Contributions Act and unemployment insurance rates are applied to only that portion of annual salaries and wages subject to the tax. Determine if the estimate reflects possible adjustments in the unemployment compensation rate.

Determine whether the projected pension costs are based on the precepts of CAS 412 and 413, bearing in mind that those standards are incorporated by reference in FAR 31.205-6, Compensation for Personal Services. Also, determine whether the payments are made quarterly in accordance with FAR 52.216-7.

J. DETERMINING FINANCIAL CAPABILITY

A contracting official must judge whether an offeror has adequate financial resources to complete the stated work. This judgment is usually based on information contained in financial statements submitted with a proposal.

These financial statements can be used during a preaward audit to develop standard financial ratios (i.e., current ratio, debt equity ratio, etc). The auditor does not have to determine the financial capability of a prospective contractor unless specifically requested to do so. However, if, during a preaward audit, the auditor discovers circumstances which raise questions about the adequacy of an offeror's financial resources to perform the work, the contracting official should be notified and a financial capability survey scheduled if necessary. See chapter 19 for a financial capability survey audit program.

K. REPORTING

As with financial and performance audits, preaward audits require a written report according to FAR 15.805-5(e).

1. Report Content. As specified in FAR 15.805-5(e), the written report should include, as a minimum, the following:

- o The findings on specific areas listed in the audit request.
- o An explanation of the basis and method the offeror used in proposal preparation. (Since this information is included in the SF 1411 package or its equivalent submitted by the contractor, audit comments may be restricted to exceptions taken to the contractor's explanation.)
- o An identification of the original proposal and of all subsequent written, formal, and other identifiable submissions by which cost or pricing data were either submitted or identified.
- o A description of any cost or pricing data that were not submitted but that may significantly affect the proposed cost or price.
- o A list of any cost or pricing data submitted that are not accurate, complete, or current and of any unsupported cost representations.
- o The originals of all technical analyses received by the auditor and a quantification of the dollar effect of the technical analyses' findings.
- o If the offeror's estimating methods or accounting system is believed inadequate to support the proposal or to permit satisfactory administration of the contemplated contract, a statement to that effect.
- o A statement of the extent to which discrepancies or mistakes of fact in the proposal have been discussed with the offeror. (Per the FAR 15.805-5, conclusions or recommendations should not be discussed with the offeror unless the contracting officer specifically requests the auditor to do so.)

The objective of the audit and the written report is to aid contracting officials in negotiating a fair and reasonable price for the proposed work. If significant weaknesses are noted in the accounting or estimating system during a pricing proposal audit, such weaknesses should be explained in the report. If the weaknesses noted are not significant or do not affect proposed prices, they should not be reported as part of the preaward audit results. Instead, they should be held over for the next accounting system review.

2. Report Format and Timeliness. A written report should be prepared similar to exhibit B (A:AM15EXB.WPF). Exhibit C (AM15EXC.WPF) shows variations to the basic preaward report. General reporting guidance is contained in chapter 14. To meet the established time frame for negotiation and contract award, the written report needs to be submitted to the contracting official by the promised date indicated in the request acknowledgement.

3. Verbal Reporting. The audit results may be conveyed verbally as soon as the field work has been completed and an exit conference held with the

offeror. To the extent feasible, a verbal report should summarize the audit determinations regarding costs and include other matters that will be covered in the written report.

4. Transmittal Letter. An example of an appropriate transmittal letter for preaward audit reports is included as exhibit D (A:AM15EXD.WPF).

L. ATTENDANCE AT PRICE NEGOTIATIONS

The auditor may be asked to attend price negotiations on large, complex proposals. Knowledge gained during the audit places the auditor in a unique position to aid a Government negotiating team in developing its negotiation objectives. Also, negotiations can be unpredictable. If supplementary information is presented during negotiations, the auditor can examine it promptly and judge its merits and impact on proposed prices.

The auditor must be prepared to respond to questions concerning any aspect of the offeror's cost or pricing data or the accounting or estimating system. Workpapers and permanent files need to be complete, current, and well referenced to facilitate responsiveness. Requests for auditors working under commercial contract to attend negotiations should be coordinated with an AIGA representative.

PERTINENT PORTIONS OF
Cost Accounting Standards (CAS)
401 AND 402

The following excerpts from CAS 401 and 402 are furnished to provide auditors with a general knowledge of the CAS consistency requirements. When applying these standards to specific situations auditors should review the entire contents of the standards, particularly the preface and the illustrations.

A. CAS 401 - CONSISTENCY IN ESTIMATING, ACCUMULATING AND REPORTING COSTS

1. 401.40 Fundamental requirement.

a. A contractor's practices used in estimating cost in pricing a proposal shall be consistent with his cost accounting practices used in accumulating and reporting costs.

b. A contractor's cost accounting practices used in accumulating and reporting actual costs for a contract shall be consistent with his practices used in estimating costs in pricing the related proposal.

c. The grouping of homogeneous costs in estimates prepared for proposal purposes shall not per se be deemed an inconsistent application of cost accounting practices under paragraphs (a) and (b) of this section when such costs are accumulated and reported in greater detail on an actual cost basis during contract performance.

2. 401.50 Techniques for application.

a. The standard allows grouping of homogeneous costs in order to cover those cases where it is not practicable to estimate contract costs by individual cost element or function. However, costs estimated for proposal purposes shall be presented in such manner and in such detail that any significant cost can be compared with the actual cost accumulated and reported therefor. In any event, the cost accounting practices used in estimating costs in pricing a proposal and in accumulating and reporting costs on the resulting contract shall be consistent with respect to: (1) the classification of elements or functions of costs as direct or indirect; (2) the indirect cost pools to which each element or function of cost is charged or proposed to be charged; and (3) the methods of allocating indirect costs to the contract.

b. Adherence to the requirement of 401.40(a) of this standard shall be determined as of the date of the award of the contract, unless the contractor has submitted cost or pricing data pursuant to Public Law 87- 653, in which case adherence to the requirement of 401.10(a) shall be determined as of the date of final agreement on price, as shown on the signed certificate of current cost or pricing data. Notwithstanding 401.40(b), changes in established cost accounting practices during contract performance may be made when authorized by the standards, rules, and regulations issued by the CASB.

B. CAS 402 - CONSISTENCY IN ALLOCATING COSTS INCURRED FOR THE SAME PURPOSE**1. 402.40 Fundamental requirement.**

All costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives. No final cost objective shall have allocated to it as an indirect cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included as a direct cost of that or any other final cost objective. Further, no final cost objective shall have allocated to it as a direct cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included in any indirect cost pool to be allocated to that or any other final cost objective.

2. 402.50 Techniques for application.

a. The fundamental requirement is stated in terms of cost incurred and is equally applicable to estimates of costs to be incurred as used in contract proposals.

b. The disclosure statement to be submitted by the contractor will require that he set forth his cost accounting practices with regard to the distinction between direct and indirect costs. In addition, for those types of cost which are sometimes accounted for as direct and sometimes accounted for as indirect, the contractor will set forth in his disclosure statement the specific criteria and circumstances for making such distinctions. In essence, the disclosure statement submitted by the contractor, by distinguishing between direct and indirect costs, and by describing the criteria and circumstances for allocating those items which are sometimes direct and sometimes indirect, will be determinative as to whether or not costs are incurred for the same purpose. Disclosure statement as used herein refers to the statement required to be submitted by contractors as a condition of contracting as set forth in Part 351 of this chapter.

c. In the event that a contractor has not submitted a disclosure statement, the determination of whether specific costs are directly allocable to contracts shall be based upon the contractor's cost accounting practices used at the time of contract proposal.

d. Whenever costs which serve the same purpose cannot equitably be indirectly allocated to one or more final cost objectives in accordance with the contractor's disclosed accounting practices, the contractor may either: (1) Use a method for reassigning all such costs which would provide an equitable distribution to all final cost objectives, or (2) directly assign all such costs to final cost objectives with which they are specifically identified. In the event the contractor decides to make a change for either purpose the disclosure statement shall be amended to reflect the revised accounting practices involved.

e. Any direct cost of minor dollar amount may be treated as an indirect cost for reasons of practicality where the accounting treatment for such cost is consistently applied to all final cost objectives, provided that such treatment produces results which are substantially the same as the

EXAMPLE OF TRANSMITTAL MEMORANDUM OF
BUFF COVER REPORT AND FINANCIAL AUDIT REPORT

DATE: Month 1, 199X

REPLY TO

ATTN OF: IG-XX

SUBJECT: Report on "Title of Audit"

TO: Appropriate DOE Official

We audited (subject and location). The specific objectives of the audit were to determine whether ...

The audit disclosed ...

Your comments on the draft report indicated (concurrence or nonconcurrence) with the recommendations. The details of management and auditor comments are set forth on pages ... of the report.

In accordance with DOE Order 2320.2B, "Establishment of Departmental Position on Inspector General Reports," the Department is requested to provide a Departmental position on the recommendations in the report. Paragraph 8.f and Attachment 1 of the order describe the procedures for preparing and processing the Departmental position. The reply is due to the Chief Financial Officer 70 days from the date of this report.

We appreciate the cooperation of your staff throughout this audit, including the attention given to resolving the findings in the report.

(Name), Manager

Regional Audit Office
Office of Inspector General

Attachment

cc: Director, Audit Liaison Division (CR-33)

EXAMPLE OF TRANSMITTAL MEMORANDUM FINAL REPORT PACKAGE
(USE MEMORANDUM PAPER)

DATE: Month 1, 199X

REPLY TO

ATTN OF: IG-XX

SUBJECT: Final Report Package for "Title of Audit"

TO: (Name), DAIG/AO

Attached is the required final report package on the subject audit. The pertinent details are:

1. Staff days: Programmed ____ Actual ____

(Explanation for difference)

2. Elapsed days: Programmed ____ Actual ____

(Explanation for difference)

3. Names of OIG audit staff:

Assistant Regional Manager:
Audit Director:
Auditor-in-Charge:
Audit Staff:

4. Names of Contractor audit staff, if any:

Audit Director:
Auditor-in-Charge:
Audit Manager:
Audit Staff:

4. Matters to be brought to attention of the IG or AIGA:

(Name), Manager
____ Regional Audit Office
Office of Inspector General

Attachments:

1. Final Report (3) (Other than blue cover report)
2. Executive Summary (2) (Blue cover report only)
3. Monetary Impact Report
4. Fact Sheet (2)
5. IGDBMS File Printout

MONETARY IMPACT OF REPORT NO. _____

1. Title of Audit: _____

2. Region/office: _____
3. IGDEMS No.: _____
4. Type of Audit: (Definitions and examples of audit types are found in the Yellow Book, pages 2-1 thru 2-5.)

5.

FINDING		BETTER USED			QUESTIONED COSTS			MGT. POSITION	POTENTIAL BUDGET IMPACT	
(A) No.	(B) Title	(C) One Time	Recurring			(G) Ques- tioned Portion	(H) Unsup- ported Portion	(I) Total	(J) C=Concur N=Noncon U=Undec.	(K) Y=Yes N=No
			(D) Amount	(E) No. Yrs.	(F) Total Amount					
TOTALS--ALL FINDINGS									XXXXXXXX	XXXXXXXX

6. Remarks: _____
7. Contractor _____
8. Contract No. _____
9. Task Order No. _____
10. Approvals:
- Regional Manager _____
- DAIG/AO _____

Instructions for Preparing Monetary Impact Report

This report provides a synopsis of the monetary impact pertaining to the audit. The dollar amount of the saving (\$) contained in the monetary impact report should tie directly to the audit report. The monetary impact report will be prepared by the audit team responsible for the report for all audits, including those prepared under contract. Add the report number to the heading and use the following instructions in completing the remainder of the form.

1. Title of Audit. The complete report title as it appears on the report cover.
2. Region/Office. The identity of the region and the audit office.
3. IGDBMS Number. Enter the assigned number.
4. Type of Audit. Check the type and sub-type as appropriate. If Financial was checked, indicate in the Remarks section if this was a certification of the financial statements.
5. Matrix. This item is designed to collect various information related to the details of the reports. The monetary impact of financial, performance and certain financial related audits should be classified as "better used" and/or "questioned cost" as appropriate. Instructions for each column follow:
 - a. Number and Title of Findings (Col A and B) - The number, of course, applies to multi-findings reports and reflects the sequential number assigned to the individual findings in the body of the report. The title of the finding will be the exact language used for the heading of the finding.
 - b. Better Used (Col C thru F) - The amount of estimated cost avoidances or increased efficiency or effectiveness which can be realized if DOE managers adopt and implement the audit recommendations to improve their operations or systems. These savings could result in deobligation of funds in the current year and/or budgetary reduction in future years. Note that "better used" amounts have not been spent.

Column C: The estimated amount of savings that can be achieved one time by implementing the recommendation. Note that the impact of preaward audits (both questioned and unsupported) should be entered in this category as separate entries with each amount identified as either (Q) for questioned or (U) for unsupported.

Column D,E,F: The estimated amount of recurring savings that can be achieved yearly. If life expectancy of the audited entity cannot be identified, use one year. If the life can be determined, use the life expectancy up to five years.

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- c. Questioned Costs (Col G thru I) - An incurred cost is questioned because (1) of alleged violation of a provision in the law, regulation, contract, grant, or cooperative agreement; (2) lack of adequate documentation to support the cost, (3) it is not allocable to Government work on the basis of benefits received; or (4) the expenditure of funds was unnecessary or unreasonable.
Note that questioned costs based on any of the above four reasons resulting from performance audits of operations being performed by DOE contractors should be reported in this category. Also Note that "questioned" amounts have been spent.

Column G: The costs that are questioned because of reasons (1), (3), and (4) of the above paragraph. Note that in general recommended recoveries from performance audits should be included in this sub-category identified with a (R) at the end of the amount.

Column H: Incurred cost that is questioned because such costs are not supported with adequate documentation and should be in the subcategory "Unsupported," as required by the IG Act of 1988.

Column I: The sum of G and H.

- d. Management Position (Col J) - This column will be used to reflect management's concurrence (C) or nonconcurrence (N) with the amounts being reported. If known, please indicate the amount being reported that management disagrees with.
- e. Budget Impact (Col K) - A determination whether the monetary impact can be potentially be used to reduce current or future years' budgets. In general, the potential amount to be reduced should come from the "Better Used" category.
6. Remarks. This section shall be used to provide any additional pertinent information regarding management's position and to bring to the attention of Headquarters any matters of special importance regarding the monetary impact.
7. Contractor. If the audit was done by an audit services contractor, the name of the contractor will be entered on this line.
8. Contract No. The number of the contract under which the work was done will be entered on this line.
9. Task Order No. The specific task order authorizing the contractor to do the work will be entered here.
10. Approvals. Designated officials and signature of approval.

FACT SHEET
AUDIT REPORTS SUBMITTED TO AIGA

1. Type of Report
 Blue Cover _____
 Buff Cover _____
 Letter _____
 Other (Specify) _____
2. Report No. _____
 3. IGDBMS No. _____
 4. Date Issued _____
 5. Audit Category _____
6. Title: _____
7. Location of Contractor or Activity: _____
8. Audit done by: AIGA _____ IPA _____ Cost _____ E or F _____
9. Type of Audit:
 Financial _____ Performance _____
 Financial Statement _____ Economy & Efficiency _____
 Financial Related (Specify Type) _____ Program Audit _____
10. Coordination with Investigations:
 Discussed with _____
 Date _____
 Disposition:
 No investigative potential _____
 Referred to _____
 Date of Referral Memo _____
11. Workpaper and Report Quality Control:
 W/P Review: AIC _____ Date: _____ Audit Dir.: _____ Date: _____
 Report Ref: Initial: _____ Date: _____ Final: _____ Date: _____
12. Savings:

Better Used				Questioned Cost Incurred			Poten. Budget Impact
One Time	Recurring		Total Amount	Questioned Portion	Unsup-ported Portion	Total	Y=Yes N=No
	Amount Per Year	No. Yrs.					

	OA		Contractor (IPA)	
	Staff Days	Elapsed Days	Staff Days	Elapsed Days
13. Original Program	_____	_____	_____	_____
14. Revision (Date: _____)	_____	_____	_____	_____
Revision (Date: _____)	_____	_____	_____	_____
15. Actual	_____	_____	_____	_____
16. Difference (13-14)	_____	_____	_____	_____
17. Total Days Suspended	_____	_____	_____	_____

18. Explanation of Overruns in Staffdays and/or Elapsed Days, and Suspensions:

19. Project Cross-Indexing:

a. _____	k. _____
b. _____	l. _____
c. _____	m. _____
d. _____	n. _____
e. _____	o. _____
f. _____	p. _____
g. _____	q. _____
h. _____	r. _____
i. _____	s. _____
j. _____	t. _____

(Enter key words on additional page, if necessary.)

20. Narrative of Report:

21. Submitted By: _____ Date: _____

22. AO Review By: _____ Date: _____

Instructions for Preparing the
Audit Report Fact Sheet

The Fact Sheet provides a synopsis of relevant information pertaining to the audit. It will be prepared for all audits, including those prepared under contract, by the audit team responsible for the report. The following instructions apply:

1. Type of Report. Check the appropriate line identifying the type of report being submitted.
2. Report No. Enter the report number assigned.
3. IGDBMS No. Enter the assigned job number.
4. Date Issued. Enter the date on the report.
5. Audit Category. Enter the major audit category as described in the IGDBMS Manual.
6. Title. Enter the complete title as it appears on the report cover or as identified in a Letter report.
7. Location of Contractor Activity. Enter the geographical location(s) where the audit was actually performed.
8. Audit done by: AIGA ____ IPA ____ Cost ____ E or F _____. Enter the name of the regional office or the name of the IPA who performed the audit. In cases where both AIGA and IPA personnel performed the audit, identify all AIGA regions and IPA firms involved. Enter the total task order(s) cost associated with the work performed on the audit. Costs will include all presurvey/survey efforts pertaining to the resultant audit. If final cost are available indicate "F;" if final costs are not available, enter "E" for estimated and use the latest actual billed amount plus an estimated for the unbilled portion.
9. Type of Audit. Check the appropriate line or identify the type of audit if "Other" is checked.
10. Coordination with Investigations. Based on this discussions with AIGI staff, enter the determination made that (1) release will not compromise possible investigations, or (2) the report was referred to AIGI staff for further review. If the report is referred, that fact should be documented by a referral memo. Enter the addressee and date of the referral memo.
11. Workpaper and Report Quality Control. Enter the name of the workpaper reviewer, report referencer, and dates when review was accomplished.
12. Savings. Enter the data from the total line of item 5 on the Monetary Impact Report.

13-18.

These sections indicate the planned and actual staff days (both AIGA and contractor) for the job. If overruns were incurred or the job was suspended, detailed explanation of the reasons for the conditions should be provided. The information is important to AIGA management; therefore, care must be taken to record and accumulate the data consistently and correctly. Elapsed days are calculated from the entrance conference date through the report date. Data should agree with Audit Project Summary Report.

19. Project Cross-Indexing. Enter key words and phrases associated with the project. Examples: "Acme Corporation," "Jones," "Fraud," and "Grant," etc. At the inception of an audit, this information shall be loaded into the IGDBMS. Upon completion of the audit, this information must be updated by the regional office.
20. Narrative of Report. The basic purpose of the narrative is to summarize the audit for OIG management. Therefore, this section must be concise and complete in all factual matters. For a contract, preaward or grant audit, indicate the type of audit, what goods or services are being purchased, the amounts of questioned, unsupported and/or unresolved costs, and the general basis for such a determination. For all other audits, indicate what was audited and provided sufficient information on each finding, including recommendations and monetary impact, for a reader unfamiliar with the subject to understand what was found.
21. Submitted By ____ Date _____. Name of the responsible audit manager who prepared the fact sheet and the date prepared.
22. AO Review By ____ Date _____. To be added by the AO staff member who reviewed the report and related fact sheet.

OFFICE OF THE INSPECTOR GENERAL
AUDIT PROJECT SUMMARY REPORT (APS)

11/24/93

Audit-No: A93PR036 Title: BNL ADMINISTRATION OF SDB PROGRAM

Milestones:	PLANNED			ACTUAL
	PROFILE	END OF SURVEY	REVISED	
ENTRANCE CONFERENCE:	01-OCT-92	02-DEC-92	02-DEC-92	02-DEC-92
SURVEY COMPLETED:	04-DEC-92	05-FEB-93	05-FEB-93	05-FEB-93
TF&R'S ISSUED:		14-JUN-93	10-AUG-93	10-AUG-93
DRAFT REPORT ISSUED:		02-AUG-93	10-AUG-93	10-AUG-93
EXIT CONFERENCE:		18-AUG-93	10-AUG-93	10-AUG-93
COMPLETED WITH REPORT:	30-AUG-93	30-JUL-93	30-JUL-93	25-AUG-93
ELAPSED DAYS:	333	240	240	266
STAFF DAYS:	150	130		210

DATE SUSPENDED: DATE TERMINATED:
DATE REACTIVATED: DATE CANCELLED:
NO OF DAYS SUSPENDED: REPORT NUMBER: ER-L-93-09

***** AUDIT CODES AND PERSONNEL *****

IG-OFFICE: PRA PRINCETN AUD TASK-NO: - -
AUDIT-TYPE: EAE ECONOMY & EFFICIENCY
CATEGORY: MPA MULTIPROGR. ACTIVITY AD: 115 STRONCZER
DOE-ORG: CHO CHICAGO OPERATIONS O AIC: 444 BOZARTH
MAJ-ISSUE: 009 PROCUREMENT AND GRAN HDQ-MON: 544 ACTON
SITE: SSA SINGLE-SITE AUDIT ARM: 101 CONNOR

**** ATC INFORMATION ****

ATC Rank ATC Description
B01A 1.0 THE CONTRACTORS PROCUREMENT PRACTICES ARE IN ACCORDANCE WITH

**** FACILITY/LOCATION INFORMATION ****

Code	Description	Location
BNL	BROOKHAVEN NATIONAL LABOR	BROOKHAVEN NATIONAL LABORATORY, NY

***** TASK INFORMATION *****

TASK-ORDER-DATE: CO TECH. REP:
ORIG-AUTH-HOURS: ORIG-AUTH-COSTS:
CURRENT-AUTH: CURRENT-AUTH-CST:
TOT-ACTL-IPA-HR: TOT-ACTL-COST:

***** TIME CHARGES *****

Emp/Cont Name	No.-Days	Last-Date	Emp/Cont Name	No.-Days	Last-Date
BOZARTH	125.6	30-OCT-93	STRONCZER	13.8	30-OCT-93
CONNOR	1.3	04-SEP-93	FLYNN	52.4	04-SEP-93
TERZINI	12.8	15-MAY-93	SIMPKINS	1.3	20-MAR-93
NARLIS	3.1	26-DEC-92			
TOTAL:	210.3				

CHAPTER 12ASSURING A QUALITY REPORTA. SCOPE OF CHAPTER

This chapter sets forth the policies and practices for assuring that OA issues quality reports.

B. REVIEW OF WORKPAPERS

General procedures for workpaper review are provided in chapter 7. However, procedures of particular importance include the following.

1. The AIC responsible for the assignment should review all workpapers for compliance with OA standards and prescribed procedures--before supervisory review and referencing begins--to assure that all papers are properly prepared and cross-indexed and the work has been adequately accomplished. AICs should indicate their review by initialing and dating the papers.

2. Workpapers should be reviewed by the AIC's immediate supervisor, usually an Audit Director. An ARM should provide this review if the Audit Director is the AIC. As a minimum, the supervisor should review sufficient workpapers to express an opinion on the adequacy of the workpapers (see also chapter 7). The supervisor's review should be made before the report is referenced and the exit conference. The supervisor's comments should be recorded on a review sheet, signed, and dated. All review notes should be retained as a part of the working paper files.

C. REVIEW OF REPORTS

The report review function is performed by Audit Directors, and Regional and Headquarters staff, and is essential to the overall quality of an audit report.

1. Regional Review. Effective supervisory review by the audit director and regional staff is essential to the overall quality of an audit report. Early supervisory participation in the audit planning process helps to focus and sharpen the audit objectives and thus the reporting objectives. Generally, the supervisor can provide a broader perspective on such matters as the reasonableness of the objectives in view of OA policies and practices and the anticipated reaction to the report by various auditees. As the audit progresses, supervisory input may help to determine the type of report to be issued and assist in identifying additional data needed to substantiate and refine the findings, or to sharpen recommendations. Supervisory agreement is required in making the final decision on whether, and to what organizational level, the report will be issued (see chapters 4, 6, and 7.)

2. Headquarters Review. Reports which are to be forwarded to Headquarters for review prior to issuance include

- o All stages of Blue Cover reports (including TF&Rs);

- o Draft reports specifically designated by the AIGA, including all draft reports of a critical/sensitive nature, i.e., congressional interest, significant public interest, or national security implications, and
- o All Management Alerts.

The purpose of the Headquarters review is to ensure (1) quality reports, (2) continuity and consistency of reports and recommendations, and (3) compliance with OA and OIG reporting policies. The Reports Review Checklist, shown in exhibit A (A:AM12EXA.WPF), will be used in the Headquarters review process. All review comments will be coordinated with the DAIG/AO, who will inform the appropriate Regional Manager of any questions or suggested changes to be made to the report. Any difference of opinion between the Regional Managers and Headquarters will be resolved as quickly as possible. When a satisfactory agreement cannot be reached, the matter will be referred to the AIGA for resolution.

3. Documenting Changes Made by Reviewers. Where report drafts are significantly changed as a result of Regional or Headquarters review, the reasons for such changes must be documented in the workpapers. Where applicable, the workpapers should contain reference to relevant audit standards. For example, if the Scope and Methodology section of a Blue Cover report is changed by a Headquarters reviewer to more closely adhere to Yellow Book standards, a notation to that effect should be included in the workpapers. This process assures that there is a documented rationale for significant changes from one draft to the next.

D. CROSS-INDEXING REPORTS

The AIC should follow specific steps in preparing a report for referencing.

1. Workpaper and report cross-indexes are to be placed on reports by the person who prepares the report. The AIC is responsible for ensuring that all portions of the report have been properly cross-indexed.

2. To the extent practicable, specific supporting evidence in the workpapers is to be identified by placing a single vertical line in the margin of the workpaper along side the evidence. Also, "highlighting" or "underlining" may be used. In any event the auditor should cross-index material to the report with a capital "R" or stating "To Report."

3. A workpaper cross-index should be repeated where there is one or more intervening cross-indexes.

4. All cross-indexes will normally be to a specific page of a workpaper--e.g., A1, p. 1. If it is necessary to cross-index a statement (sentence or phrase) to more than one workpaper or to more than one page in a workpaper, the specific pages should be identified--i.e., A1, pp. 1 & 6, not A1-A6.

5. The report cross-index should be placed directly opposite the statement to which it relates. Lines may be drawn across the page to delineate where the statement begins and ends to which the cross-index applies.

6. All figures, amounts, dates and titles appearing in the report must be supported by identical figures or amounts in the workpapers. Also, a referencer should not have to perform computations to determine how a reported figure was computed. For example, in support of a statement that "four of the seven (57 percent) T&A reports did not have the required attachments," the cross-index may be referred to such entries as;

- o 3 reports had the required attachments, and
- o 4 reports did not have the required attachments.

However, the referencer should not have to add the "3" and "4" to get support for the "7." That calculation should be reflected in the workpapers. Likewise, the workpaper should contain computations for "57 percent." Normally, calculations should be carried out to a greater degree of accuracy than the figure cited in the report--e.g., $4 / 7 = 57.1$ percent (rounded) = 57 percent. In addition, a separate cross-index would be needed to support that the attachments were "required."

7. Whenever factual material is repeated in a draft report, it is desirable to cite other pages in the report for support rather than repeatedly citing the same supporting workpapers. This situation may frequently occur in the "Finding" paragraphs where the same information is normally repeated under the "Details of Finding." Likewise, material in the "Observations and Conclusions" section of a report may be the same as that in "Finding" paragraphs. Citing other pages with the same information allows the referencer to carry forward the referencer's mark on material already verified. It may also aid in identifying redundant statements.

8. Auditors should avoid citing a large number of cross-indexes to support a single statement. If several cross-indexes are needed to support a statement, a separate workpaper summary should be prepared which ties together the various pieces of information needed to support a finding or conclusion. However, the workpaper summary must be cross-indexed, factual items traced to source, and computations verified.

E. REFERENCING

The referencing process is another essential step in assuring overall audit report quality. Referencing is defined as the verification of factual data, the determination of the reasonableness of the conclusions reached in view of the factual data provided, and the practicality of the recommendations made in an audit report. All audit reports will be independently referenced. Where administratively feasible, referencing will be performed by an audit staff member who is grade GS-12 or above. For Blue Cover Reports or other reports with significant or controversial findings, preferably, an auditor at grade GS-13 or above should be selected as the referencer. The referencer must not have any management responsibility for the audit nor have participated in the audit. The purposes of referencing are:

- o To verify the accuracy of all facts stated in the report and make a determination as to whether the working papers adequately support the findings, conclusions and recommendations; and
- o To review the soundness and clarity of the report's presentation.

Referencing is to be completed before the official draft report is staffed (see chapter 11) within the Department. (Do not reference the TF&R, which is issued before the official draft.) Referencing does not relieve supervisors of their responsibilities for reviewing workpapers or determining whether the report complies with all prescribed reporting policies and requirements.

The following matrix summarizes the versions of the report requiring cross-indexing and referencing.

<u>Before Release Of</u>	<u>Document Must Be</u>	
	<u>Cross-Indexed</u>	<u>Referenced</u>
TF&R	Yes	No
Official Draft	Yes*	Yes
Final Report*	Yes*	Yes*

- * Only those changes made after the official draft was referenced.

The referencer represents the Regional Manager, who is responsible for the report. The referencer, although not responsible for the report itself, is responsible for determining that:

- o Every figure and statement of fact is supported by satisfactory evidence in the workpapers or by mathematical or clerical checks. This includes:
 - Checking each figure and statement of fact for consistency within the report and to the supporting workpapers; and
 - Independently verifying the accuracy of each total, percentage or similar figure in the report.
- o The report findings, conclusions and recommendations are logical, sound, clearly presented and adequately supported by workpapers.

1. Referencing Documentation. At the start of the referencing process, the referencer will be given a completely cross-indexed copy of the report and all supporting workpapers.

The referencer should use the updated version of Referencer's Review Sheets and is encouraged to use word processing techniques when filling out

the sheets with reference comments (see exhibit B, A:AM12EXB.WPF). These sheets serve as a record of the comments raised by the referencer, their consideration by the audit staff, and their final disposition. The referenced report and the Referencer's Review Sheets should be retained in the workpapers.

2. Referencing Procedures. Referencing consists of three distinct phases. These are: (1) general familiarization with the report to be referenced and the underlying support; (2) detailed referencing; and (3) resolution and disposition of the comments raised during the referencing process.

a. General Familiarization - The referencer should first scan the underlying source material to obtain a general understanding of the organization of the workpapers.

The general familiarization phase provides referencers with the opportunity to identify any restrictions that will affect the referencing process and will necessarily qualify their work. For example, certain support may not be available in the workpapers since it is to be provided by a headquarters branch or another regional office. These restrictions should be noted by the referencer on the Referencer's Review Sheet. However, they must be resolved before the referencing is complete.

b. Detailed Referencing - During the detailed referencing phase, the referencer checks every fact, figure, date, title, etc., in the written product to the underlying support to determine its accuracy and to ensure that it is consistently used.

(1) Important items of information in the report--contract numbers, quotations, dollar amounts, interpretation of contract terms, paraphrasing of policy, law, or regulation, etc.--should be checked to copies of the original source documentation in the workpapers.

(2) The referencer's review is independent and based on the referencer's own knowledge and logic. The referencer should question the adequacy of supporting documentation included in the workpapers when warranted regardless of supervisory review. If the opinions, conclusions and recommendations are not consistent with the factual material examined, which received supervisory review, the referencer should record his/her dissenting view.

(3) Lead schedules and summaries may be used as support if the information on them has been cross-indexed and traced and verified to the original source. The referencer should trace selected items to the source indicated to assure that the information is factual and correct. To the extent that the referencers test workpaper summaries and lead schedules, they should "tick" off on that information the same as for the report being referenced.

(4) The referencer should indicate acceptance that each sentence of the report is supported by placing a referencer's tick mark (~) at the left-hand margin of each line (see exhibit C, A:AM12EXC.WPF). Every figure, date, proper name, title, address, and each word of a quotation will

be referenced by placing a tick mark (~) immediately over it. In addition, each handwritten word inserted must be ticked. The referencer should use a different color pencil than was used for indexing or by other reviewers.

(5) All computations should be checked by the referencer and marked (~) to indicate that the computation has been independently verified.

(6) Material referenced only to an interview will require qualification in the report by a phrase such as "we were informed", depending on the circumstances.

(7) The referencer should record all points, questions and suggestions on a Referencer's Review Sheet, spaced so that comments on the disposition can be made without crowding (see exhibit D, A:AM12EXD.WPF).

The suggested way of cross-indexing comments on the review sheet to the report is to place the report page number and the referencer's symbol (a circled 1, 2, 3, etc.,) on the Referencer's Review Sheet opposite the comment. The referencer's symbol is then noted on the report next to the statement relating to the comment, as illustrated in exhibit D (A:AM12EXD.WPF).

(8) The referencer should verify that adequate support is contained in the workpapers for all reported facts. The referencer should scan each workpaper cited as support to see if there are any conditions or qualifications that would affect the validity of the workpaper. All references must be to the workpapers, including copies of pertinent sections of documents, published reports, or other published documents. For example, if DOE Order 2100.1A is cited as support, the appropriate pages should be copied and placed in the workpapers. When support for a reported fact is not located in the cited workpapers, the referencer should immediately write a reference note and proceed with the remainder of his review.

(9) The referencer should not normally spend time searching through the workpapers if a cited reference does not provide the needed support. However, if referencers are aware that an uncited workpaper may contain the needed information, they should note this in their reference note (e.g., their note may state that a particular fact is not supported by the cited reference, and identify the specific workpaper that may contain the needed information).

(10) When referencing classified material, referencers should check the classification of each paragraph to the source documents unless the audit staff plans to have the Department reclassify the draft at a later date. In the latter case, referencers should note in their comments that they have not verified the classifications. Referencing comments should also be classified as appropriate for proper security.

(11) In referencing computer-generated data, the referencer has two major considerations: (1) How far to go in referencing computer programs written by OIG staff; and (2) the extent to which the reliability of computer-generated data should be assessed.

ABC represented that it is not subject to CAS coverage (Public Law 91-379) on the basis that it is not currently performing any CAS covered national defense contracts valued at \$10 million or greater and that such contracts do not amount to 10 percent or more of total sales.

2. CAS Does Apply and No Violations Were Noted.

ABC represented that it is subject to [full] or [modified] CAS coverage (Public Law 91379). Our audit of the proposal disclosed that it complied with CAS.

3. CAS Does Apply and Violations Were Noted.

ABC represented that it is subject to CAS coverage (Public Law 91- 379). Our audit of the latest CAS disclosure statement, dated April 30, 1989, disclosed that ABC's method of proposing hourly rates for engineering materials and supply costs differed from its method of accumulating, recording, and reporting these costs. The use of engineering materials and supply hourly rates for estimating purposes results in noncompliance with CAS 401, Consistency in Estimating, Accumulating, and Reporting Costs.

OR

ABC is not required to file a disclosure statement, but rather is subject to modified CAS coverage, CAS 401, Consistency in Estimating, Accumulating, and Reporting Costs, and 402, Consistency in Allocating Costs Incurred for the Same Purpose. Our audit disclosed that ABC's method of proposing areawide midpoint labor rates differed from its method of accumulating, recording, and reporting actual labor costs. The use of areawide midpoint labor rates for estimating results in noncompliance with CAS 401.

ABC increased material costs by 3 percent for freight, but could not support this factor with accounting, statistical, or other relevant data, as required by CAS 401, Interpretation No. 1.

Include a recommendation that DOE inform the offeror of its failure to comply with CAS and require the offeror to revise its cost estimating method.

F. COSTS INCURRED UNDER THE PROPOSED CONTRACT

Only two cases exist: either the offeror has or has not incurred costs to date. Examples of report language follow.

1. No Costs Have Been Incurred.

ABC personnel represented that no costs had been incurred under the proposed contract as of February 16, 1990.

2. Costs Have Been Incurred.

ABC is performing the proposed work under a cost-plus-fixed-fee letter order. ABC represented that costs incurred through November 30, 1989, are as follows:

Direct labor	\$ 50,500
Fringe benefits (at 30%)	15,150
Overhead (at 54.1%)	35,517
Other direct costs	<u>3,500</u>
Total	<u>\$104,667</u>

The scope of our audit did not include an audit of incurred costs. Accordingly, we do not express a conclusion or any other form of assurance on the incurred costs as of November 30, 1989.

G. RECOMMENDATIONS

Recommendations correspond to the accounting system weaknesses listed in the section titled Accounting System Review.

We recommend that the DOE contracting officer require ABC to:

1. Prepare invoices from the general ledger.
2. Use actual hours worked to compute effective labor rates for exempt personnel.
3. Establish written travel, purchasing, and fixed asset depreciation policies and procedures.
4. Require employees to prepare and sign timesheets in ink and authorize all changes.
5. Refine its chart of accounts to clearly identify allowable, unallowable, direct, and indirect costs.
6. Separate financial and accounting duties so that persons who sign checks do not maintain accounting records.
7. Discontinue the practice of signing blank checks.

**EXAMPLE OF TRANSMITTAL LETTER
FOR PREAWARD AUDIT REPORT
(USE MEMORANDUM PAPER)**

DATE: Month 1, 199X

REPLY TO

ATTN OF: IG-XX

SUBJECT: Preaward Audit of ...

TO: Requester

In response to your request, attached are two copies of the subject report.

The Office of Inspector General (OIG) has no objection to the release of this report at the discretion of the contracting officer to the duly authorized representatives of the contractor.

Under the provisions of Title 32, Code of Federal Regulations, Part 290.26(b)(2) (as amended August 10, 1977), all Freedom of Information Act requests for audit reports received by the OIG will be referred to the cognizant contracting officer for determination as to releasability and a direct response to the requestor.

Information contained in this audit report may be confidential. The restrictions of 18 U.S.C. 1905 should be considered before this information is released to the public.

Also attached is a list of all names and classes of persons who had access to the subject report and/or information contained therein.

Please provide us with a copy of the memorandum of negotiation, pursuant to Federal Acquisition Regulation 15.808(b). If any further information is required, we will furnish it on request.

(Name), Manager

Regional Audit Office
Office of the Inspector General

Attachment

cc: Director, Audit Liaison Division (CR-33)

CHAPTER 16AUDIT OF INCURRED COSTS**A. SCOPE OF CHAPTER**

This chapter applies to any audit of costs incurred under Government prime contracts or subcontracts. For convenience, reference in the chapter may be limited to use of the word "contract" which encompasses subcontracts in the context of cost incurred audits.

B. OBJECTIVES OF AN AUDIT OF INCURRED COSTS

Incurred costs are audited to ascertain whether they are properly allocable to the contract, reasonable in amount, and allowable under applicable laws and regulations, contract terms and conditions, cost principles (contained in the FAR, DEAR, and CAS), and generally accepted accounting principles and practices.

The criteria employed in making these determinations include written advance agreements, generally accepted accounting principles, the contract cost principles and procedures, other pertinent contract provisions, the CAS applicable in the circumstances, and negotiation memoranda, which may document specific intent of the parties as to certain financial aspects of the contract. The pricing proposal used in negotiations is also a valuable audit tool.

Types of contracts requiring audit of costs incurred include:

- o Cost, no fee
- o Cost sharing
- o Cost plus fixed fee
- o Cost plus award fee
- o Cost plus incentive fee
- o Fixed price incentive fee
- o Time and material
- o Labor hour

Additionally, termination claims involve verification of incurred costs. Such claims can arise under any type of contract, including a firm fixed price contract. Chapter 19 contains specific guidance for auditing termination claims.

C. BACKGROUND

The total cost of a cost-reimbursable contract is the sum of the allowable direct and indirect costs allocable to the contract, less any allocable credits. The contract price consists of the total cost as described above plus a negotiated profit or fee.

Each contract contains a ceiling amount which cannot be exceeded. This restriction limits the Government's liability. Since the ceiling amount is developed before the work is done, it is based on estimates of the total allowable costs plus the negotiated amount for profit or fee. The ceiling amount may initially cover payments pertaining to a specified period or phase of the work, rather than the entire scope of work and the total contemplated contract period. Incurred costs will vary from estimated costs. Costs claimed in excess of contract estimated costs are unallowable. The contracting officials decide whether a contract will be modified to provide additional funds to cover a cost overrun.

D. AUDIT APPROACH AT LARGE CONTRACTORS

Where multiple Government contracts are in force, the approach to auditing incurred costs will likely be to perform: (1) an interim audit encompassing the period costs of all multiyear contracts and (2) a closeout audit of each completed or terminated contract. The interim audit provides for timely resolution of cost and accounting problems, finalizes contract costs to a specified date, and expedites the closeout audit at contract completion. The closeout audit and accounting settlement are the final accounting of the reimbursement paid to the contractor. If interim audits were made of the total costs incurred, the closeout audit should be limited to summarizing the results of completed interim audits.

The amount of testing and verification required at a particular contractor location is influenced by (1) the extent and result of prior audit experience, (2) the reliability of the system of internal controls and the auditor's related vulnerability assessment, and (3) the significance of the costs to be audited compared to the total costs of all work for the audit period. The examination of transactions and procedures must be sufficient to support a conclusion as to the allowability of costs charged to Government contracts. If the cost accounting system was recently reviewed, the results will influence the extent of testing and the nature of the verification required to develop a conclusion on the allowability of incurred costs.

E. NOTIFICATION TO AIGA REPRESENTATIVE OF UNUSUAL CIRCUMSTANCES

Notify the AIGA representative promptly when:

- o Fraud or other unlawful activity is suspected or
- o Access to essential records is restricted or denied.
- o See chapter 4 section D for details.

F. GUIDANCE FOR AUDIT OF DIRECT AND INDIRECT COSTS

The contractor should have prepared a claim covering direct costs incurred and indirect costs allocated to each Government contract requiring audit. The program for review and testing is developed based on the contractor's claim or claims, applying the guidance provided in the following sections.

Each claim should summarize billings and payments made under each contract. Identify any instances where claimed costs are in excess of the contract price.

If precontract costs are claimed, assure that they meet allowability requirements and have been approved in the contract provisions or in advance agreements. Similarly, assure that costs claimed do not include costs incurred after the contract expiration date.

1. Reconciliation of Costs Claimed. For each contract, reconcile the total amount billed, including fee, with the present claim and on to the contractor's books. Determine whether the billed amount, as well as the claimed amount, is within the amount obligated under the contract. If the audit ultimately substantiates costs incurred, plus fee, in excess of the amount obligated under a contract, the audit report should question the amount in excess of funds currently obligated and include a footnote stating the amount which would be allowable if the contract were modified to authorize reimbursement of the overrun.

2. Purchased Materials and Services. The audit objectives of a direct material and services audit are to determine whether the costs charged to Government contracts are allocable to the contracts and if the materials were purchased at reasonable prices, in reasonable quantities, and are properly accounted for. In addition, the auditor should determine the adequacy of the contractor's policies, procedures, and internal controls applicable to material costs.

a. Sampling Transactions - When the value of purchased material and services is significant, measure the reliability of the accounting charges to Government contracts by sampling for attributes. Stratifying purchases by dollar amounts or by other factors that will best serve in forming a conclusion about the costs incurred will be helpful. If significant material transactions are from stock inventory, the attribute sampling program will include stock issues and returns. By sampling transactions, verify that

- o material charged to a Government contract was consistent as to type and quantity needed for the contract work, as evidenced by priced bills of material, requisitions, and comparison with information considered during contract negotiations;
- o the material was received and paid for, as evidenced by receiving reports, stores inventory receipts and issues, original vendor invoices, and cancelled checks;
- o the prices paid were reasonable as evidenced by the price analysis/competitive bids contained in purchasing files;

- o the material was actually used on Government contract work, as evidenced by production work orders or fabrication records, or was otherwise accounted for as residual inventory, scrap, or spoilage;
- o associated costs of material purchases, such as freight and material handling, were reasonable and charged on a basis consistent with the contractor's standard practices, and these types of costs were not double counted.

Attribute sampling may disclose a need for a deeper review and evaluation of one or more of the following functional areas: purchasing, warehousing and inventory control, control and disposition of scrap, and spoiled and obsolete materials.

b. Indicators of Findings - Situations such as the following may be noted through physical observations and examination of records. It is important to ascertain whether a given situation resulted in unnecessary or increased costs to the Government. This listing is illustrative, rather than all inclusive.

- o Prohibited procurement practices observed (example: cost plus-a-percentage-of-cost subcontract).
- o Inadequate price justification for interorganizational transfers.
- o Unaudited cost-reimbursable subcontracts for services or material.
- o Significant differences between costs per the priced bills of material, actual material costs, and information provided during contract negotiations.
- o Evidence of in-house fabrication of parts and components previously purchased from others.
- o Subcontracting of engineering work to a greater extent than initially proposed.
- o Higher scrap and spoilage factors than estimated at the time of contract negotiations.
- o Disposition not made of scrap and spoiled materials.
- o Amounts received from sale of scrap or receipts improperly credited.
- o Unreasonably large residual inventory or inventory under poor physical control.
- o Failure to credit the contract with residual inventory items normally stocked by the contractor.

- o Failure to return damaged and defective materials to suppliers for credit.
- o Lack of accountability over returnable containers or inadequate record of deposits.

3. Incurred Labor Costs. The objective of the examination of labor charges is to assure that labor costs charged to Government contracts are properly allocable and that the amounts are reasonable and allowable in accordance with contract terms and applicable regulations. Meeting this objective involves using audit procedures designed to insure that the labor effort was actually expended, that charges were not manipulated, and that labor rates paid were commensurate with employees' skills and the type of work performed. Tests made should cover direct labor as well as indirect labor allocated to Government contracts.

The following sections provide audit procedures for reviewing the labor charging system, for conducting a floor check, and for making payroll tests. Certain additional procedures can be used to evaluate the reliability of the labor distribution records and the effectiveness of labor usage. For example, if labor utilization reports are available, compare the utilization rate in departments having principally Government work with those of departments working on commercial work. Review labor utilization trends and determine to what extent management is measuring and monitoring productivity. If utilization reports are unavailable, the auditor should, where appropriate, review procedures established to (1) estimate and monitor the target cost of project work orders, (2) assign classes of personnel to projects to determine whether they are being assigned according to required skills, (3) control the phase-out operations of a project, and (4) control idle time. In short, the objective of these audit steps is to determine whether the employees are being used effectively. Technical assistance would generally be required to accomplish these steps.

a. Labor Charging Systems and Floor Checks - Labor charging systems and floor checks should be reviewed while Government contract work is in progress, not after the work is completed. If an auditor is not in residence at the contractor's facility, a separate, unannounced visit may be made for this purpose.

If the contractor has an independent timekeeping system, review its procedures and controls and evaluate the extent of its independence. In this regard, remember that the employees should charge their time to project orders. Supervisors should approve employee timesheets but not be authorized to insert the project order numbers. Also, responsibilities should be divided between personnel preparing time and job cost records, personnel responsible for operating within budgets, and personnel preparing the payroll.

Review procedures for checking on employees arriving late or leaving early. If a clock-in system is used, observe whether employees clock in or out for each other. Using a list of employees assigned to a specific department or work area, account for the status of each employee on the list through physical observation. Add the names of other employees working in the

area to the list. Record the work project and cost code for each employee observed by examining pertinent work orders. Obtain explanations about the nature of the work where questions arise about the cost code being charged.

Determine the reasons for any timekeeping or job charging discrepancies noted, e.g., differences between names on the list and clock cards in the rack, employees at work who are not on the control list, employees on the control list who are missing, reasons for time being charged to work which is not being performed, reasons for idleness, and reasons for working outside assigned job classifications.

Where the number of workers appears excessive or it appears that the workers are used inefficiently, obtain explanations from the contractor.

Compare results of observations with the recorded labor distribution for the period audited.

Where payrolls and labor distribution records show that overtime is consistently being used on Government work, make a separate floor check during a period of scheduled overtime work. Evaluate controls exercised over the authorization and scheduling of overtime work and whether productivity is being carefully monitored in the extra pay periods. The previously outlined audit procedures for floor checks can also be applied here if warranted.

If overtime premiums are being charged direct to Government work, determine whether this practice is followed on commercial work. If labor charges observed during floor checks differ markedly from labor costs subsequently charged to contracts and/or if controls are considered unsatisfactory, consult with the AIGA supervisor or representative before undertaking further work.

b. Payroll Tests - The same period selected for labor observations and labor distribution should be used to examine payroll preparation practices.

Reconcile the gross payroll with the total labor cost distributed for the period. Compare payroll payments to approved time records and job cost distribution cards, cancelled checks, and personnel records (for approved job classifications and pay rates and department assignments). Inquire into all alterations of time records and job cost records. Examine approval of payments exceeding the maximum rate for the assigned classification.

Determine whether any labor categories were charged directly to Government contracts contrary to the accounting treatment accorded similar categories on commercial work. Also determine whether the labor categories being charged direct to contracts were proposed in the same manner.

Determine the propriety of journalized adjustments to recorded labor distribution charges.

4. Other Direct Costs Incurred. The following should be considered when examining other direct costs incurred.

a. Consistency of Accounting Treatment - When items are charged to a Government contract as other direct costs, the contractor's procedures should provide for like or comparable items to be similarly charged to other work. Review the contract pricing proposals, negotiation memoranda, and contract provisions to ascertain whether costs being claimed as direct were intended to be classified that way. Test transactions to ascertain whether similar costs of commercial work are also classified as direct charges.

b. Other Purchases - Test transactions for other purchases being charged as other direct costs in much the same way as purchased material and services were tested.

c. Professional and Consulting Fees - Professional and consulting fees charged directly to contracts should be identified in initial pricing proposals and should be authorized in the contract document. Many contractors subcontract for, rather than hire, engineering and other technical personnel. This practice should be carefully reviewed if the subcontracts extend over prolonged periods and/or they involve a large number of personnel. The auditor should (1) compare the hourly rate costs to contractor's personnel in like labor categories, (2) ascertain the type of contracts, i.e., fixed price, cost-reimbursable, commercial, etc., they are assigned to, (3) determine how the effort they are accomplishing was proposed to the Government, and (4) consider how the costs are recorded in the accounts, i.e., as other direct charges to the contract or as direct labor. If the subcontracted work is being performed in the contractor's plant, under the contractor's supervision, an assessment of overhead may be appropriate.

Consultant fees should be traced to reports submitted by the consultants and the work accomplished evaluated to determine whether the fees paid were reasonable and allocated to Government work.

d. Travel and Subsistence - Test travel and subsistence costs against source documentation to establish whether (1) the costs were incurred directly for contract work by direct labor employees; (2) the costs are allowable according to the contract cost principles and conform to the contractor's travel policy; and (3) there is evidence of control over the number of trips, the frequency and duration of trips, and the number of employees traveling together to the same destinations.

e. Relocation of Employees - Examine relocation costs charged directly or indirectly to the Government for allowability under the contract terms and cost principles. Note that voluntary resignation by an employee within 12 months after relocation will require that the contractor credit the Government for any reimbursed relocation expenses (FAR 31.205-35(d)).

f. Telephone Toll Charges - Where telephone toll calls are charged directly, ascertain whether the system for recording and classifying each toll call is consistently applied throughout that contractor's operation and yields equitable results. In many cases, phone calls are not sufficiently accounted for to demonstrate allowability, and auditors may require additional information from the auditee.

g. Royalties - The propriety of charging royalty costs direct to a contract should have been covered in an advance agreement. If it was not,

review the contractor's price proposal and/or related negotiation memorandum to see if the costs were considered acceptable contract charges. If an audit determination still cannot be made, the matter should be discussed with the contracting officer to see whether the Government has license free use of the controlling patent.

h. Computer Costs - In many cases computer costs are accumulated in a separate cost center and allocated to both direct and indirect cost objectives. If automated data processing capability is extensive and diverse, the algorithm developed for allocating costs can be complex. Usually, to evaluate computer costs charged to contracts, it is necessary to:

- o verify that algorithm components accurately determine whether all applicable costs are included in the development of the coefficients (i.e., manpower costs, programming costs and hardware costs) and whether profit is excluded,
- o review benchmark tests performed to validate the algorithm,
- o ascertain whether controls to record all use of computer resources are adequate, and
- o ascertain whether the billing algorithm is current and represents current equipment usage.

Where smaller computers do not have software routines to collect user information, examine the contractor's justification for any direct charges to Government work.

5. Incurred Indirect Costs. A detailed explanation of the review of indirect costs appears in chapter 17. Indirect costs claimed for final cost purposes must be based on the lesser of rates negotiated for each fiscal year or the ceiling rates specified in the contract. A listing of final negotiated indirect cost rates for each fiscal year and the Government contract activity bases to which the final negotiated rates apply should be kept in the permanent file.

G. SPECIAL CONSIDERATIONS, OTHER FORMS OF CONTRACTS

Auditors should pay special attention when performing labor hours verifications, material cost verifications, total cost comparisons, and underrun of costs reviews.

1. Labor Hours Verification - Labor Hour Contracts and Time and Material Contracts. The following tests should be performed during a labor hours verification.

a. Verify labor hours billed to job cost records and approved time records. Assure that the number of overtime hours worked are not inflated in the billing. For an interim audit of labor hours billed, consider making a floor check to establish the propriety of the charges.

b. Ascertain whether labor hours billed were charged by individuals who are regularly and consistently classified as direct labor and

whether their job classifications are consistent with the classifications contained in the initial price proposal.

c. If the contract permits classifications of personnel normally charged as indirect labor to be charged direct, ascertain whether the overhead and/or general and administrative expense rates were appropriately adjusted so that the costs were not double counted.

d. Ascertain whether the actual ratio of time applied to the contract by employees in each skill level approximates the ratio included in the negotiated contract or proposal. Investigate cases where time charged by employees earning lower salaries than the average contained in the pricing proposal was considerably more than proposed or negotiated.

e. Overtime involving premium pay should be compared in much the same way as the salary levels.

f. If, after accomplishing the above audit steps, evidence indicates that the contract may have been defectively priced, the auditor should contact the AIGA supervisor or representative to discuss the feasibility of performing a defective pricing review.

2. Material Cost Verification - Time and Material Contracts. The following steps should be performed to verify material costs.

a. Ascertain whether billed material costs include a handling charge. If so, assure that this charge is not also in the overhead factor included in the labor hour rate.

b. Test the prices of billed material and subcontract costs where they constitute a significant amount of the total contract costs. Ascertain whether billed items are allocable to the contract by reviewing codings on purchase orders, material withdrawal tickets, bills of material, etc.

c. Assure that applicable discounts and expense credits such as unserviceable parts, scrap, or excess inventory have been offset against billed costs. Bear in mind that materials must be billed at cost.

d. Where subcontract work is billed on a unit rate basis, ascertain the reasonableness of the rate, e.g., the rate paid to the subcontractor for regular commercial work or to the contractor's personnel with the same labor classifications.

3. Total Cost Comparison - Labor Hour Contracts and Time and Material Contracts. Compare the total job costs per books with the total amount billed less the profit factor which was negotiated as part of the labor hour rates. Where the total actual costs are significantly less than the costs billed (i.e., the total billed amount less the negotiated profit factor), examine the job cost history more closely and compare it to the original estimate for each element of cost to discern whether the estimate was misleading or erroneous as a basis for establishing the contract rates.

4. Underrun of Costs - Incentive Contracts. Where total actual costs on incentive contracts are significantly less than the estimated costs used in

setting the target cost, inquire into the reasons for the variance and, if discernible, include the explanations in the report. Some of the actions which could cause costs to vary widely are

- o Overstatement of cost elements due to defective pricing or unforeseen developments;
- o Engineering changes resulting in unanticipated cost reductions, contingencies which did not materialize;
- o Changes to the proposed make-or-buy patterns of major components;
- o Cost accounting system changes; and
- o Indirect expense allocations larger than anticipated.

Conversely, it would also be valuable for contracting officials to know what caused a large cost overrun of the target cost.

H. REPORTING

Audits of direct or indirect cost during an accounting periods are called interim audits.

1. Interim Audits. The report on an interim audit of incurred costs should be prepared using the format in exhibit A (A:AM16EXA.WPF) as a guide for complex audits. Exhibit B (AM16EXB.WPF) shows a format for a less complex report. Exhibit C (AM16EXC.WPF) contains some possible variations to these reports. Chapter 14 contains certain general reporting guidance. In the examples shown, the reports are concerned with only one contract. Where interim reports are to be provided for more than one contract, a separate exhibit showing Contractor's Claimed Costs and Audit Results should be prepared for each contract.

An interim report normally covers one accounting period. When more than one accounting period is involved, the costs should be shown separately by accounting periods. This breakdown allows for the application of annual indirect expense rates for each period and is especially important where indirect rates have not been finalized at the time of the audit.

At smaller contractor locations, interim audit reports will normally be issued following the completion of direct cost audits and audits of proposed indirect expense rates which are normally accomplished simultaneously. Therefore, questioned overhead costs will be based on rates that have not been negotiated. The report should include an exhibit showing Claimed Indirect Expense Rates and Audit Results. The schedule should provide sufficient details to permit the contracting officer to understand the bases for the contractor's claimed rates, the bases for questioned costs, and any other information required to negotiate final overhead rates.

Costs which have not been audited (subject to assist audits) should be clearly identified and classified as unresolved and appropriately explained.

2. Final Audits. The report on a final (close out) audit should normally be prepared using exhibit A as a guide. The auditor is normally requested to make a final cost audit when costs have not been fully audited and resolved. In such cases the detailed results of the audit of costs incurred in the final year(s) not previously audited should be presented in the report, as with interim reports, along with exhibits (if appropriate) showing Claimed Direct and Indirect Expense Rates and Audit Results. In addition, an exhibit should be included summarizing the entire contract.

3. Transmittal Letter. An example of an appropriate transmittal letter for incurred cost audit reports is included as exhibit D (A:AM16EXD.WPF).

I. CLOSING OF COMPLETED CONTRACTS

Contract periods do not necessarily coincide with the contractor's fiscal year. When a contract is completed in the first part of a fiscal year and the direct costs are not significant, the contracting official may decide to expedite cost settlement and close the contract without waiting until the next regular incurred cost audit. In such cases the direct costs of the period can be audited separately. The contracting officer can negotiate indirect costs on the basis of either of the following methods, depending on which is most indicative of current conditions.

- o The final rates agreed to for the prior fiscal year.
- o The provisional billing rate for the current period.

EXAMPLE OF COST INCURRED AUDIT REPORT

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITSREPORT ON THE INDEPENDENT FINAL AUDIT OF
CONTRACT NO. DE-AC12-345678901
SEPTEMBER 25, 1985, TO NOVEMBER 15, 1987
XYZ CORPORATION
CITY, STATE

REPORT NO:

PURPOSE AND SCOPE

In response to a request from the U.S. Department of Energy (DOE), Office of Procurement Operations, we performed a final audit of the costs claimed by XYZ Corporation under Contract No. DE-AC12345678901. The costplus-fixed-fee contract covered the periods September 25, 1985, to September 1, 1987, and October 8 to November 15, 1987, and provided for XYZ to perform support services for the ... program. From September 25, 1985, to November 15, 1987, XYZ claimed \$473,202 plus a \$32,017 fee.

The costs claimed are the responsibility of the contractor, XYZ Corporation. Our responsibility is to reach a conclusion on the costs claimed, based on our audit.

The purposes of the audit were to determine the allowability of costs claimed under the contract and to verify level-of-effort direct productive manhours expended under the contract. Allowable costs are costs incurred that are reasonable, allocable, and in accordance with the terms of the contract, applicable cost principles, laws and regulations, and generally accepted accounting principles and practices appropriate to the particular circumstances.

The direct cost audit scope was limited to test procedures for validating XYZ's claimed costs by tracing them to books of original entry and supporting records. We tested specific transactions, but did not evaluate XYZ's total internal control system or technical aspects of its performance.

The indirect cost audit scope was limited to tests of indirect costs and costs comprising the allocation bases. In addition, we evaluated the appropriateness of the allocation methods used.

The direct productive manhours scope was limited to reviewing timesheets and vendor invoices to determine total direct productive manhours.

As defined in the above scope paragraph(s) we conducted our audit in accordance with generally accepted Government auditing standards that applied to this financial related audit. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the data and

records reviewed are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records reviewed. An audit also includes assessing the accounting principles used and significant estimates made by the contractor, as well as evaluating the overall presentation. Criteria used in evaluating the claimed costs also included cost principles set forth in the Federal Acquisition Regulations (FAR), DOE Acquisition Regulations (DEAR), and the Cost Accounting Standards (CAS). We believe that our audit provides a reasonable basis for our audit conclusions.

We completed our onsite work on July 26, 1990.

CIRCUMSTANCES AFFECTING THE AUDIT

We did not perform a technical review of the contract. Accordingly, audit results are qualified pending the outcome of such a review.

Based on DOE's instructions, we did not audit the Fiscal Year (FY) 1988 indirect cost rates. XYZ expects these rates to be audited as part of a large contract XYZ has with Accordingly, we classified all FY 1988 indirect costs as unresolved.

AUDIT RESULTS

Audit results are detailed in exhibits A through C and are summarized below:

	<u>Questioned Costs</u>	<u>Unresolved Costs</u>
09/25/85 to 03/31/86	\$15,656	
04/01/86 to 03/31/87	64,901	
04/01/87 to 11/15/87	<u>1,797</u>	<u>\$37,663</u>
Total	<u>\$82,354</u>	<u>\$37,663</u>

We conclude that, except for the questioned and unresolved costs summarized above and described in the notes to exhibits A through C, the costs represent fairly the allowable costs incurred under the contract.

Compliance with applicable laws and regulations related to the contract is the responsibility of XYZ management. As part of our evaluation, we performed tests of compliance with certain provisions of laws and regulations related to the contract. Our objective was not, however, to provide a conclusion on overall compliance with such provisions.

Except for the matters described in the notes to exhibits A through C, the results of our tests indicate that, for the items tested, XYZ complied in all material respects with the provisions of applicable laws and regulations related to the contract. For the items not tested, nothing came to our attention that caused us to believe that XYZ has not complied, in all material respects, with those provisions.

We reviewed the direct productive manhours expended in this contract. Section G of the DOE contract stipulates that the contract fixed fee will be reduced if actual direct productive manhours is less than 90 percent of the 1,178 direct productive manhours specified. XYZ claimed direct productive manhours of 923.25. XYZ's records supported employee direct productive manhours of 893.5 and temporary help direct productive manhours of 138.75, for a total of 1,032.25.

We discussed the audit results with XYZ's president, on July 26, 1990.

OTHER MATTERS TO BE REPORTED

In planning and performing our audit of costs claimed by XYZ under Contract No. DE-AC12-345678901 from September 25, 1985, through November 15, 1987, we considered its internal control structure to determine auditing procedures for the purpose of expressing our conclusion on costs claimed and not to provide assurance on the internal control structure.

XYZ management is responsible for establishing and maintaining an internal control structure that will ensure costs claimed are allowable under the contract. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure regarding allowable costs are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit preparation of costs claimed in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purposes of this report, we classified the significant internal control structure policies and procedures as those that relate to the recording and reporting of costs under Government contracts and to ensuring compliance with laws and regulations that have a material impact on costs claimed. These are control procedures designed to ensure the following:

- o The breakdown of costs within the accounting system was adequate for cost determination purposes.
- o Specific cost elements were afforded consistent treatment regarding Government and non-Government cost objectives.
- o Allowable and unallowable costs were routinely identified and segregated in the accounting system.
- o Adequate source documentation supported all costs.
- o Assets were safeguarded against loss or unauthorized use or disposition.

- o All accounting data were accurate, reliable, and traceable to underlying source documentation.
- o Contract terms and conditions were known by appropriate personnel, and the effects of contract terms and conditions were properly reflected in the accounting records.

For the internal control categories listed above, we obtained an understanding of the design of relevant policies and procedures, determined if they had been placed in operation, and assessed control risk.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions are matters coming to our attention relating to significant deficiencies in the internal control structure design or operation that, in our judgment, could adversely affect XYZ's ability to record, process, summarize, and report financial data for the contract consistent with management's assertions. These reportable conditions follow:

1. XYZ did not adequately segregate recordkeeping and check-signing responsibilities. The check signer has access to accounting records, the check book, and cash receipts.
2. XYZ did not have written accounting procedures.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to claimed costs being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control structure would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. We conclude that the first condition described above is a material weakness.

RECOMMENDATIONS

We recommend that DOE:

1. Require XYZ for future contracts to segregate accounting duties.
2. Require XYZ for future contracts to document its accounting procedures.
3. Determine to what extent, if any, the contract fixed fee should be reduced for the reduction in direct productive manhours.

CONTRACTOR'S COMMENTS

The president's comments are included in the notes to the exhibits.

JOHN DOE & COMPANY

By: _____

ACCEPTED BY:

INSPECTOR GENERAL & PAGEE

OFFICE OF

REPORT NUMBER:

Exhibit A
Page 1 of 3XYZ Corporation
City, StateClaimed Costs and Audit Results
Contract No. DE-AC12-345678901
September 25, 1985, to March 31, 1986

	<u>Contractor's Claimed Costs</u>	<u>Audit Results Questioned Costs</u>	<u>Notes</u>
Direct Labor	\$ 38,580	\$ 1,592	1
Fringe Benefits	9,579	702	2
Overhead	36,481	6,673	3
Materials and Supplies	3,482	520	4
Travel	1,635	1,583	5
General and Administrative (G&A)	<u>18,167</u>	<u>4,586</u>	6
Total Costs	<u>\$107,924</u>	<u>\$15,656</u>	

REPORT NUMBER:
NOTES TO EXHIBIT AExhibit A
Page 2 of 3

1. XYZ claimed direct labor costs of \$38,580. Timesheets and payroll records, however, supported direct labor costs of \$36,988. We questioned the \$1,592 difference.

2. We calculated questioned fringe benefit costs as follows:

Difference between claimed 24.83-percent fringe benefit rate and the 24-percent rate per audit (Schedule A-1) applied to direct labor costs ($0.83\% \times \$38,580$)	\$320
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Fringe benefits allocable to questioned direct labor costs ($24\% \times \$1,592$)	<u>382</u>
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Total	<u>\$702</u>
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3. We calculated questioned overhead costs as follows:

Difference between claimed 75.75-percent overhead rate and the 64.99-percent rate per audit (Schedule A-2) applied to direct labor and fringe benefit costs ($10.76\% \times \$48,159$)	\$5,182
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Overhead allocable to questioned direct labor and fringe benefit costs ($64.99\% \times \$2,294$)	<u>1,491</u>
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Total	<u>\$6,673</u>
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4. XYZ claimed \$520 for commercial blanket bond insurance, but could not support or explain how this insurance benefited the contract. Accordingly, we questioned these costs in accordance with FAR 31.201-4, Determining Allocability.
5. XYZ claimed \$1,583 in travel costs as the result of a yearend reallocation of charges from an indirect travel account. This reallocation was apparently based on a review of bills with XYZ's officers. The bills and accompanying receipts do not indicate the business purpose of the expenses. Because we were thus unable to determine the allocability of these expenses in accordance with FAR 31.201-4, accordingly, we questioned this amount.

REPORT NUMBER:
NOTES TO EXHIBIT A

Exhibit A
Page 3 of 3

6. We calculated questioned G&A costs as follows:

Difference between claimed 20.24-percent G&A rate and the 17.26-percent rate per audit (Schedule A-3) applied to total costs excluding G&A ($2.98\% \times \$89,757$)	\$2,675
G&A allocable to questioned costs excluding G&A ($17.26\% \times \$11,070$)	<u>1,911</u>
Total	<u>\$4,586</u>

REPORT NUMBER:

Schedule A-1

Page 1 of 2

XYZ Corporation
City, StateSchedule of Contractor's
Claimed Fringe Benefit Rate and Audit Results
April 1, 1985, to March 31, 1986

<u>Expense</u>	<u>Claimed Costs</u>	<u>Audit Results</u> <u>Questioned</u> <u>Costs</u>	<u>Notes</u>
Sick Leave	\$ 4,833		
Holiday Leave	10,870		
Annual Leave	23,568		
Other Labor	781		
Employer Federal Insurance Contribution Act (FICA)	28,648		
Health Insurance	14,001		
Employee Life Insurance	1,437		
Workers' Compensation Insurance	1,728		
Unemployment Compensation	2,683		
Miscellaneous Fringe Benefits	2,065	\$1,165	1
Administrative Leave	2,156		
Employee Relocation Travel	<u>1,995</u>	<u>1,995</u>	2
Total	<u>\$ 94,765</u>	<u>\$3,160</u>	
 <u>Allocation Base</u>			
Total Labor	<u>\$381,655</u>		
Claimed Rate	<u>24.83%</u>	<u>0.83%</u>	
Rate per Audit	<u>24%</u>		3

REPORT NUMBER:
NOTES TO SCHEDULE A-1

Schedule A-1
Page 2 of 2

1. Miscellaneous fringe benefits included a \$1,165 adjustment to the employee advances account. XYZ could not provide documentation to support the allocability of this charge to the fringe benefit pool in accordance with FAR 31.201-4.
2. XYZ claimed relocation costs of \$1,995 incurred in moving a newly hired employee. These relocation costs should be allocated as overhead costs in accordance with FAR 31.203(b), Indirect Costs, and accordingly are questioned.
3. We calculated the fringe benefit rate per audit as follows:

Fringe benefits (\$94,765 minus \$3,160)	\$ 91,605
Labor costs	<u>\$381,655</u>
Fringe benefit rate per audit (\$91,605 divided by \$381,655)	<u>24%</u>

REPORT NUMBER:

Schedule A-2

Page 1 of 4

XYZ Corporation
City, State

Schedule of Contractor's
Claimed Overhead Rate and Audit Results
April 1, 1985 to March 31, 1986

<u>Expense</u>	<u>Claimed Costs</u>	<u>Audit Results</u>	
		<u>Questioned Costs</u>	<u>Notes</u>
Indirect Labor	\$ 84,321	\$ 1,298	1
Fringe Benefits	20,937	1,012	2
Consultant Fees	(383)	617	3
Travel	15,886	15,504	4
Copying Service	859		
Printing, Binding and Typesetting	945		
Telephone	15,272		
Books and Periodicals	(34)		
Other Equipment Rental	3,046		
Equipment Repairs and Service	3,556		
Expendable Supplies	4,683		
Expendable Furniture	285		
Office Space Rent	49,009		
Lodging Offsite	6,743	6,743	5
Other Office Repairs and Service	1,830		
Casualty/Liability Insurance	620		
Depreciation Expense	9,086		
Amortization Expense	149		
Postage	903		
Delivery/Messenger Service	2,131		
Professional Societies	950		
Temporary Help	848		
Seminar/Lunches and Refreshments	14,038	12,234	6
Miscellaneous	31	(1,995)	7
Dues/Licenses	399		
Property taxes	<u>651</u>	<u> </u>	
Total	<u>\$236,761</u>	<u>\$35,413</u>	
<u>Allocation Base</u>			
Total Direct Labor and Fringe Benefits	<u>\$304,505</u>	<u>\$(5,308)</u>	8
Claimed Rate	<u>77.75%</u>	<u>12.76%</u>	
Rate per Audit	<u>64.99%</u>		9

NOTE: Figures in parentheses are increases.

REPORT NUMBER:
NOTES TO SCHEDULE A-2

Schedule A-2
Page 2 of 4

1. XYZ recorded an employee's salary for one pay period as overhead. The timesheet to support these costs indicated that the employee worked on other activities during the pay period, resulting in overclaimed indirect labor costs of \$1,298.

2. We calculated questioned fringe benefits of \$1,012 as follows:

Difference between claimed 24.83-percent fringe benefit rate and the 24-percent rate per audit (Schedule A-1) applied to labor costs (0.83% x \$84,321)	\$ 700
---	--------

Fringe benefits allocable to questioned labor costs (24% x \$1,298)	<u>312</u>
---	------------

Total	<u>\$1,012</u>
-------	----------------

3. XYZ claimed \$617 for a business development consultant, but did not have a written agreement with this consultant. We were thus unable to assess the allowability and allocability of the fees in accordance with FAR 31.205-33, Professional and Consultant Service Costs.

4. We calculated questioned travel costs of \$15,504 as follows:

- a. XYZ claimed \$11,004 in travel costs as the result of a yearend reallocation of bills after reviewing these bills with XYZ's officers. The bills and accompanying receipts did not indicate the business purpose of the expenditures, and we could not assess the allocability of these charges to the overhead pool, in accordance with FAR 31.201-4.

- b. XYZ paid each of its officers \$250 a month for out-of-pocket expenses for 6 months in Fiscal Year 1986, or \$4,500 total for the year. The officers did not retain receipts or otherwise account for their expenditures. We questioned these costs as unsupported.

5. XYZ claimed \$6,743 paid for an employee's apartment rent while he managed a farm for the company. We questioned this expense, because it is a direct charge and unallocable to the overhead pool in accordance with FAR 31.203(a).

REPORT NUMBER:
NOTES TO SCHEDULE A-2Schedule A-2
Page 3 of 4

6. We calculated questioned seminar/lunch and refreshments costs of \$12,234 as follows:
- a. As explained in Note 4.a., we could not assess the allocability of XYZ's charges and, accordingly, we questioned \$6,008 for seminar/lunches and refreshments.
 - b. XYZ had a monthly account with a local restaurant. Invoices and receipts from the restaurant for \$4,571 did not include descriptions of the business purposes of the meals. Therefore, we could not assess the allocability of these costs in accordance with FAR 31.201-4.
 - c. XYZ reimbursed one of its officers for \$1,655 of business development expenses in Fiscal Year 1986, but could not provide documentation to support these expenses.
7. For the reasons stated in Schedule A-1, Note 2, we reclassified these costs as overhead.
8. XYZ's claimed \$304,505 allocation base included \$243,936 of direct labor costs and \$60,569 of fringe benefits. We calculated questioned direct labor and fringe benefit base costs of \$(5,308) as follows:
- a. As described in Note 1 above and in Schedule A-3, Note 1, XYZ misclassified \$5,914 of direct labor costs as overhead and G&A labor. We increased the base to include these direct labor costs.
 - b. We calculated questioned fringe benefit costs as follows:

Difference between claimed 24.83-percent fringe benefit rate and the 24-percent rate per audit (Schedule A-1) applied to direct labor costs ($0.83\% \times \$243,936$)	\$2,025
Fringe benefits allocable to questioned direct labor costs [$24\% \times \$ (5,914)$]	<u>(1,419)</u>
Total	<u>\$ 606</u>

REPORT NUMBER:
NOTES TO SCHEDULE A-2

Schedule A-2
Page 4 of 4

9. We calculated the overhead rate per audit as follows:

Overhead costs (\$236,761 minus \$35,413)	\$201,348
	<hr/>
Direct labor and fringe benefits base (\$304,505 plus \$5,308)	\$309,813
	<hr/>
Overhead rate per audit (\$201,348 divided by \$309,813)	64.99%
	<hr/>

REPORT NUMBER:

Schedule A-3

Page 1 of 2

XYZ Corporation

City, State

Schedule of Contractor's Claimed General and Administrative Rate
and Audit Results

April 1, 1985, to March 31, 1986

<u>Expense</u>	<u>Claimed Costs</u>	<u>Audit Results</u>	
		<u>Questioned Costs</u>	<u>Notes</u>
Indirect Labor	\$ 53,398	\$ 4,616	1
Fringe Benefits	13,259	1,551	2
Consultant Fees	3,000	3,000	3
Professional Fees and Services	33,260	460	4
Local Travel	1,234		
Other Computer Expenses	3,591		
Out-of-City Travel	5,749	5,310	5
Copying Service	4,094		
Printing, Binding, and Typesetting	1,076		
Telephone	1,835		
Books and Periodicals	366		
Other Equipment Rental	819		
Equipment Repairs and Service	638		
Expendable Supplies	565		
Expendable Furniture	51		
Office Space Rent	8,690		
Other Office Repairs and Service	304		
Casualty/Liability Insurance	831		
Other Recruiting Services	414		
Depreciation Expense	1,630		
Amortization Expense	27		
Postage	332		
Delivery/Messenger Service	519		
Temporary Help	4,885		
Seminar/Lunches and Refreshments	6,038	5,743	5
Miscellaneous	708		
Dues/Licenses	316		
Property Taxes	117		
State Corporate Taxes	100		
Total	\$147,846	\$20,680	
<u>Allocation Base</u>			
Total Cost Excluding G&A	\$730,394	\$(6,167)	6
Claimed Rate	20.24%	2.98%	
Rate per Audit	17.26%		7

NOTE: Parentheses indicate a cost increase.

REPORT NUMBER:
NOTES TO SCHEDULE A-3Schedule A-3
Page 2 of 2

1. XYZ recorded the salaries of two of its officers for one pay period as G&A. The timesheets to support these costs indicated that the employees worked on some direct activities during the pay period, resulting in overclaimed indirect labor costs of \$4,616.

2. We calculated questioned fringe benefits as follows:

Difference between claimed 24.83% fringe benefit rate and the 24% rate per audit (Schedule A-1) applied to labor costs (0.83% x \$53,398)	\$ 443
---	--------

Fringe benefits allocable to questioned labor costs (24% x \$4,616)	<u>1,108</u>
---	--------------

Total	<u>\$1,551</u>
-------	----------------

3. XYZ claimed \$3,000 for a business development consultant, but did not have a written agreement with this consultant. We were thus unable to assess the allowability and allocability of the fees in accordance with FAR 31.205-33.
4. XYZ claimed \$460 for entertainment costs incurred by its legal counsel, which are unallowable in accordance with FAR 31.205-14, Entertainment Costs. Accordingly, we questioned these costs.
5. XYZ claimed \$5,310 for travel and \$5,743 for seminar/lunches and refreshments as the result of a yearend reallocation of bills with XYZ's officers. The bills and accompanying receipts did not indicate the business purpose of the expenditures, and we could not assess the allocability of these charges to the G&A pool, in accordance with FAR 31.201-4. Accordingly, we questioned these costs.
6. We calculated \$(6,167) of questioned total costs excluding G&A to include labor and fringe benefits questioned in Notes 1 and 2 above.
7. We calculated the G&A rate per audit as follows:

G&A expenses (\$147,846 minus \$20,680)	<u>\$127,166</u>
Total costs excluding G&A base (\$730,394 plus \$6,167)	<u>\$736,561</u>
G&A rate per audit (\$127,166 divided by \$736,561)	<u>17.26%</u>

EXAMPLE OF SHORT-FORM COST INCURRED AUDIT REPORT

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITS

FINAL AUDIT OF
COSTS CLAIMED UNDER
U.S. ENVIRONMENTAL PROTECTION AGENCY
CONTRACT NO. OST-0000-D-00-0
APRIL 7 TO OCTOBER 15, 1986
ABC, INC.
CITY, STATE

REPORT NO:

PURPOSE AND SCOPE

In response to a request from the U.S. Department of Energy (DOE), Field Office, Oak Ridge, we audited ABC, Inc's (ABC) costs claimed under Contract No. OST-0000-D-00-0 with the U.S. Environmental Protection Agency for the period April 7 to October 15, 1986. ABC provided automated data processing and office automation services. Compensation was based on fixed daily rates. ABC claimed \$30,204.

The costs claimed are the responsibility of the contractor, XYZ Corporation. Our responsibility is to reach a conclusion on the costs claimed, based on our audit.

The purpose of the audit was to determine the allowability of costs claimed under the contract. Allowable costs are costs incurred that are reasonable, allocable, and in accordance with the terms of the subcontract, applicable cost principles, laws and regulations, and generally accepted accounting principles and practices appropriate to the particular circumstances.

The audit scope was limited to test procedures for validating ABC's claimed costs by tracing them to books of original entry and supporting records. We tested specific transactions, but did not evaluate ABC's total internal control system or technical aspects of its performance.

As defined in the above scope paragraph(s) we conducted our audit in accordance with generally accepted Government auditing standards that applied to this financial related audit. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the data and records reviewed are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records reviewed. An audit also includes assessing the accounting principles used and significant estimates made by the contractor, as well as evaluating the overall presentation. Criteria used in evaluating the claimed costs also included cost principles set forth in the Federal Acquisi-

tion Regulations (FAR), DOE Acquisition Regulations (DEAR), and the Cost Accounting Standards (CAS). We believe that our audit provides a reasonable basis for our audit conclusions.

We completed our onsite work on August 29, 1989.

CIRCUMSTANCES AFFECTING THE AUDIT

We did not perform a technical review of the subcontract. Accordingly, audit results are qualified pending the outcome of such a review.

AUDIT RESULTS

Based on the audit, we take no exception to the \$30,204 claimed.

We conclude that, costs claimed represent the allowable costs incurred under the contract from April 7 to October 15, 1986.

Compliance with applicable laws and regulations related to the subcontract is the responsibility of ABC management. As part of our evaluation, we performed tests of compliance with certain provisions of laws and regulations related to the contract. Our objective was not, however, to reach a conclusion on overall compliance with such provisions.

The results of our tests indicate that, for the items tested, ABC complied in all material respects with the provisions of applicable laws and regulations related to the contract. For the items not tested, nothing came to our attention that caused us to believe that ABC had not complied, in all material respects, with those provisions.

We discussed the audit results with the controller and the accountant, on November 29, 1989.

OTHER MATTERS TO BE REPORTED

In planning and performing our audit of costs claimed by ABC under Contract No. OST-0000-D-00-0 from April 7 to October 15, 1986, we considered its internal control structure to determine our auditing procedures for the purpose of reaching our conclusion on costs claimed and not to provide assurance on the internal control structure.

ABC management is responsible for establishing and maintaining an internal control structure that will ensure cost claimed are allowable under the contract. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure regarding allowable costs are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit preparation of costs claimed in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future

periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purposes of this report, we classified the significant internal control structure policies and procedures as those that relate to the recording and reporting of costs under Government contracts and to ensuring compliance with laws and regulations that have a material impact on costs claimed. These are control procedures designed to ensure that:

- o The breakdown of costs within the accounting system was adequate for cost determination purposes.
- o Specific cost elements were afforded consistent treatment regarding Government and non-Government cost objectives.
- o Allowable and unallowable costs were routinely identified and segregated in the accounting system.
- o Adequate source documentation supported all costs.
- o Assets were safeguarded against loss or unauthorized use or disposition.
- o All accounting data were accurate, reliable, and traceable to underlying source documentation.
- o Contract terms and conditions were known by appropriate personnel and the effects of contract terms and conditions were properly reflected in the accounting records.

For the internal control categories listed above, we obtained an understanding of the design of relevant policies and procedures, determined if they had been placed in operation, and assessed control risk.

We noted certain matters involving the internal control structure and its operation that we consider reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions are matters coming to our attention relating to significant deficiencies in the internal control structure design or operation that, in our judgment, could adversely affect ABC's ability to record, process, summarize, and report financial data for the contract. These reportable conditions follow:

1. A number of timesheets were prepared in pencil. ABC's controller stated that all timesheets now are completed in pen.
2. Employees did not initial timesheet changes. ABC's controller stated that all timesheet changes now are initialed by employees.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to costs claimed being audited may occur

and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control structure would not necessarily disclose all reportable conditions also considered to be material weaknesses as defined above. We conclude that the conditions described above are material weaknesses.

RECOMMENDATION

We recommend that the DOE contracting officer, on behalf of DOE, ABC's cognizant Government agency, review ABC's revised timekeeping procedures to determine the adequacy of the changes made.

CONTRACTOR'S COMMENTS

Except as noted in the Other Matters to Be Reported section, ABC representatives did not comment on the audit results.

JOHN DOE & COMPANY

By: _____

ACCEPTED BY:

OFFICE OF INSPECTOR GENERAL

POSSIBLE VARIATIONS TO
THE BASIC COST-INCURRED AUDIT REPORT

Possible variations to the basic audit report are described in the following sections. Variations are grouped by audit report section title.

A. CIRCUMSTANCES AFFECTING THE AUDIT

Disclose in this section items outside the audit scope or items that adversely affect the audit conduct or scope and may have resulted in revised audit results. For example:

- o Reliance on approved or provisional indirect cost rates.
- o Any scope limitations, such as not performing an audit of indirect cost rates for a specific time period.
- o Unaudited subcontract costs (classified as unresolved).
- o Lack of access to records.

B. AUDIT RESULTS

This section summarizes the audit results, qualified as appropriate, and should provide the auditor's conclusion. The four conclusions that are given in audit reports:

- o Unqualified.
- o Qualified (because of questioned or unresolved costs).
- o Adverse (because of significant questioned or unresolved costs).
- o Adverse (because of significant questioned or unresolved costs and matters included in the Circumstances Affecting the Audit section of the report, if applicable).

1. Unqualified. The unqualified conclusion follows:

We conclude that costs claimed represent allowable costs incurred under the contract from July 1, 1987, to June 30, 1988.

2. Qualified.

All report sections are the same as the basic report, except for the addition of the following qualification and conclusion paragraphs (because of questioned or unresolved costs).

a. Qualification Paragraph - When summarizing audit results, use the following wording when only one exhibit is involved (or the audit results are otherwise straightforward). Use a summary table when more than one exhibit is presented in the report.

As described in the notes to exhibit A, we questioned \$100,000 and classified \$250,000 as unresolved.

b. Conclusion Paragraph -

We conclude that, except for the questioned and unresolved costs summarized above and described in the notes to exhibit A, costs claimed represent allowable costs incurred under the contract from July 1, 1987, to June 30, 1988.

3. Adverse (Because of Significant Questioned or Unresolved Costs).
When an adverse conclusion is warranted, use the following paragraphs.

a. Qualification Paragraph -

Audit results are described in the notes to exhibits A through D and are summarized below:

<u>Fiscal Year</u>	<u>Claimed Costs</u>	<u>Questioned Costs</u>	<u>Unresolved Costs</u>
1988	\$123,000	\$ 50,000	\$10,000
1989	133,000	50,000	10,000
1990	143,000	50,000	10,000
1991	<u>153,000</u>	<u>50,000</u>	<u>10,000</u>
Total	<u>\$555,000</u>	<u>\$200,000</u>	<u>\$40,000</u>

b. Conclusion Paragraph -

We conclude that, because of the questioned and unresolved costs summarized above and described in the notes to exhibits A through D, the costs claimed do not present fairly, in all material respects, the allowable costs incurred under the contract from July 1, 1987, to June 30, 1991, in accordance with the FAR, DEAR, and the terms of the contract, in conformity with generally accepted accounting principles.

4. Adverse (Because of Significant Questioned or Unresolved Costs and Matters Included in the Circumstances Affecting the Audit Section). When an adverse conclusion is warranted for these reasons, use the following paragraphs.

a. Qualification Paragraph -

Except for the effects, if any, on the costs claimed of the matters described in the Circumstances Affecting the Audit section of this report, audit results are summarized below: [Use a summary table like the one presented in No. 3 above.]

b. Conclusion Paragraph -

We conclude that, because of the effects of the matters referred to in the preceding paragraph and described in the notes to exhibit A, costs claimed do not represent allowable costs incurred under the contract from July 1, 1987, to June 30, 1988.

c. COMPLIANCE REPORTING IN A COST-INCURRED AUDIT

These paragraphs will follow the cost results in the Audit Results section of the report.

1. No Instances of Material or Immaterial Noncompliance.

Compliance with applicable laws and regulations related to the contract is the responsibility of XYZ management. As part of our evaluation, we performed tests of compliance with certain provisions of laws and regulations related to the contract. Our objective was not, however, to reach a conclusion on overall compliance with such provisions.

The results of our tests indicate that, for the items tested, XYZ complied in all material respects with the provisions of applicable laws and regulations related to the contract. For the items not tested, nothing came to our attention that caused us to believe that XYZ had not complied, in all material respects, with those provisions.

2. Instances of Both Material and Nonmaterial Noncompliance.

Compliance with applicable laws and regulations related to the contract is the responsibility of XYZ management. As part of our evaluation, we performed tests of compliance with certain provisions of laws and regulations related to the contract. Our objective was not, however, to reach a conclusion on overall compliance with such provisions.

Material instances of noncompliance are failures to follow requirements, or violations of prohibitions, contained in statutes, regulations, or the contract that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to claimed costs. The results of our tests of compliance disclosed the following material instances of noncompliance.

[Describe each instance: condition, cause, criterion, and effect; or refer to the place where the findings appear.]

In addition to these material instances of noncompliance, we also noted the following nonmaterial instances of noncompliance.

[Describe each instance: condition, cause, criterion, and effect; or refer to the place where the findings appear.]

We considered the above material instances of noncompliance in reaching our conclusion on whether XYZ's costs claimed under Contract No. XXXXXXXX from July 1, 1987, through December 31, 1988, represented allowable

costs. Because of these material instances of noncompliance, our report on costs claimed contains a [qualified/adverse] conclusion.

Except as described above, the results of our tests indicate that, for the items tested, XYZ complied in all material respects with the provisions of applicable laws and regulations related to the contract. For the items not tested, nothing came to our attention that caused us to believe that XYZ had not complied, in all material respects, with those provisions.

3. Instances of Material Noncompliance.

Compliance with applicable laws and regulations related to the contract is the responsibility of XYZ management. As part of our evaluation, we performed tests of compliance with certain provisions of laws and regulations related to the contract. Our objective was not, however, to reach a conclusion on overall compliance with such provisions.

Material instances of noncompliance are failures to follow requirements, or violations of prohibitions, contained in statutes, regulations, or the contract that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the costs claimed. The results of our tests of compliance disclosed the following material instances of noncompliance.

[Describe each instance: condition, cause, criterion, and effect; or refer to the place where the findings appear.]

We considered these material instances of noncompliance in reaching our conclusion on whether XYZ's costs claimed under Contract No. XXXXXXXX from July 1, 1987, through December 31, 1988, represented allowable costs. Because of these material instances of noncompliance, our report on those costs claimed contains a [qualified/adverse] conclusion.

Except as described above, the results of our tests indicate that, for the items tested, XYZ complied in all material respects with the provisions of applicable laws and regulations related to the contract. For the items not tested, nothing came to our attention that caused us to believe that XYZ had not complied, in all material respects, with those provisions.

4. Instances of Noncompliance that are Not Material.

Compliance with applicable laws and regulations related to the contract is the responsibility of XYZ management. As part of our evaluation, we performed tests of compliance with certain provisions of laws and regulations related to the contract. Our objective was not, however, to reach a conclusion on overall compliance with such provisions.

The results of our tests of compliance disclosed the following nonmaterial instances of noncompliance.

[Describe each instance: condition, cause, criterion, and effect; or refer to the place where the findings appear.]

We considered these nonmaterial instances of noncompliance in reaching our conclusion on whether costs claimed by XYZ under Contract No. XXXXXXXXXX from July 1, 1987, through December 31, 1988, represented allowable costs. These nonmaterial instances of noncompliance do not affect our report on costs claimed.

The results of our tests indicate that, for the items tested, XYZ complied in all material respects with the provisions of applicable laws and regulations related to the contract. For the items not tested, nothing came to our attention that caused us to believe that XYZ had not complied, in all material respects, with those provisions.

D. OTHER MATTERS TO BE REPORTED

Include the internal control reporting and any other matters that should be disclosed to the contracting officer in this section.

1. If Reportable Conditions Were Noted During the Audit and One or More of the Conditions is a Material Weakness.

In planning and performing our audit of the costs claimed under Contract No. XXXXXXXXXX by XYZ Corporation from July 1, 1987, through December 31, 1988, we considered its internal control structure to determine our auditing procedures for the purpose of reaching a conclusion on these costs claimed and not to provide assurance on the internal control structure.

XYZ's management is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of costs claimed in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purposes of this report, we classified the significant control structure policies and procedures as those relating to the recording and reporting of costs under Government contracts and to ensuring compliance with laws and regulations that have a material impact on costs claimed. These are control procedures designed to ensure the following:

- o The breakdown of costs within the accounting system was adequate for cost determination purposes.

- o Specific cost elements were afforded consistent treatment regarding Government and non-Government cost objectives.
- o Allowable and unallowable costs were routinely identified and segregated in the accounting system.
- o Adequate source documentation supported all costs.
- o Assets were safeguarded against loss or unauthorized use or disposition.
- o All accounting data were accurate, reliable, and traceable to underlying source documentation.
- o Contract terms and conditions were known by appropriate personnel and the effects of contract terms and conditions were properly reflected in the accounting records.

For the internal control categories listed above, we obtained an understanding of the design of relevant policies and procedures, determined if they have been placed in operation and we assessed control risk.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions are matters coming to our attention relating to significant deficiencies in the internal control structure design or operation that, in our judgment, could adversely affect an organization's ability to record, process, summarize, and report financial data consistent with management's assertions for costs claimed. These reportable conditions are as follows:

Reportable Conditions

[Include numbered paragraphs describing the reportable conditions noted. Each reportable condition description should contain condition, cause, criterion, effect, and recommendation.]

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the costs claimed being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control structure would not necessarily disclose all reportable conditions and, accordingly, would not necessarily disclose all reportable conditions also considered to be material weaknesses as defined above. We conclude that the first three conditions [OR AS APPROPRIATE] described above are material weaknesses.

2. If Reportable Conditions Were Noted During the Audit and None of the Conditions is Material. All paragraphs are the same as item one above, except the last paragraph. Wording for the last paragraph follows.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to costs claimed being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control structure would not necessarily disclose all reportable conditions and, accordingly, would not necessarily disclose all reportable conditions also considered to be material weaknesses as defined above. We believe, however, that none of the reportable conditions described above is a material weakness.

3. If No Reportable Conditions Were Noted During the Audit.

In planning and performing our audit of costs claimed under Contract No. XXXXXXXXXX by XYZ Corporation from July 1, 1987, through December 31, 1988, we considered XYZ's internal control structure to determine our auditing procedures for the purpose of reaching a conclusion on costs claimed and not to provide assurance on the internal control structure.

XYZ's management is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of costs claimed in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purposes of this report we classified the significant control structure policies and procedures as those relating to the recording and reporting of costs under Government contracts and to ensuring compliance with laws and regulations that have a material impact on costs claimed. These are control procedures designed to ensure that:

- o The breakdown of costs within the accounting system was adequate for cost determination purposes.
- o Specific cost elements were afforded consistent treatment regarding Government and non-Government cost objectives.
- o Allowable and unallowable costs were routinely identified and segregated in the accounting system.
- o Adequate source documentation supported all costs.

- o Assets were safeguarded against loss or unauthorized use or

E. RECOMMENDATIONS

Make a recommendation to correct each internal control weaknesses identified as well as matters of noncompliance as appropriate. For example:

We recommend that the DOE contracting officer require XYZ to:

1. Strengthen internal control by requiring a timely independent bank reconciliation.
2. Comply with CAS 402.

EXAMPLE OF TRANSMITTAL LETTER
FOR INCURRED COST AUDIT REPORT
(USE MEMORANDUM PAPER)

DATE: Month 1, 199X

REPLY TO

ATTN OF: IG-XX

SUBJECT: Incurred Cost Audit of...

TO: Requester

In response to your request, attached are two copies of the subject report.

The Office of Inspector General (OIG) has no objection to the release of this report at the discretion of the contracting officer to the duly authorized representatives of the contractor.

Under the provisions of Title 32, Code of Federal Regulations, Part 290.26(b)(2) (as amended August 10, 1977), all Freedom of Information Act requests for audit reports received by the OIG will be referred to the cognizant contracting officer for determination as to releasability and a direct response to the requestor.

Information contained in this audit report may be confidential. The restrictions of 18 U.S.C. 1905 should be considered before this information is released to the public.

Please provide the details of the resolution of audit findings. If any further information is required, we will furnish it on request.

(Name), Manager

Regional Audit Office
Office of the Inspector General

Attachment

cc: Director, Audit Liaison Division (CR-33)

CHAPTER 17AUDIT OF INDIRECT COSTS**A. SCOPE OF CHAPTER**

This chapter discusses audits of indirect costs allocated to Government prime contracts or subcontracts.

B. OBJECTIVES OF AN INDIRECT COST AUDIT

The primary objectives of an indirect cost audit are to determine whether the indirect costs allocated to a contract are consistent with the benefits received by the contract and whether the indirect costs are reasonable and allowable, according to the contract cost principles.

C. BACKGROUND

Indirect costs are costs which benefit the contract but which are not incurred directly for the contract. These costs are normally allocated through the application of indirect cost rates. Examples of indirect costs are overhead expenses, general and administrative expenses, bid and proposal expenses, independent research and development expenses, and home office expenses.

1. Most contracts contain provisions which specifically address the treatment of indirect costs. The most common type of contract provision permits the contractor to bill for indirect costs at provisional rates subject to subsequent adjustment to final negotiated rates. Most costreimbursable contracts require the contractor to calculate and submit to the contracting officer proposed final indirect cost rates 90 days after the end of each fiscal year. The contracting officer normally requests an indirect cost audit of these rates before they are negotiated and finalized.

2. Another type of contract provision, used for educational institutions' contracts and grants, allows the contractor to bill for indirect costs at a predetermined rate established before the costs are incurred.

3. Some contracts and grants with States and municipalities have a "carry forward provision." An indirect cost rate relating to a time period is established before the start of the period. If the actual negotiated indirect costs for the period are more or less than the amount obtained from using the fixed rate, the difference is carried forward and included in the rate computation for the following year.

4. Other contracts have provisions which permit recovery of actual indirect costs up to an amount based on applying a maximum ceiling rate. Ceiling rates set an upper limit on the amount of indirect cost which may be billed. Ceiling rates are established when a contractor has insufficient data to budget indirect costs accurately or when significant fluctuations in business volume may occur.

5. Contractors and the Government may enter into advance agreements for forward pricing rates to reduce the time and effort required to perform detailed evaluations of indirect cost rates on each proposal. The auditor generally reviews the contractor's advance agreement proposal to determine if the projections used contain reasonable expectations of the future operations. The auditor must review these rates periodically to determine if the circumstances under which they were developed have changed.

D. PREDETERMINED OVERHEAD RATES

If overhead is billed at predetermined rates, no review is required other than verifying that the proper rates and allocation bases were used and that the computation of allocable indirect costs was correct.

E. GENERAL STEPS - INCURRED INDIRECT COST AUDITS

The examination of incurred indirect cost allocations to Government contracts should include the following steps:

- o The scope and extent of the audit is influenced by (1) the dollar volume of Government business as compared to the contractor's total business volume, (2) the dollar volume of cost-reimbursable contracts, and (3) the results of prior audits of the cost accounting system and incurred costs, tempered by any accounting changes. Analyze the proposed allocation bases to obtain information on the extent of the Government's participation in the contractor's indirect costs.
- o Review and verify the clerical accuracy of the contractor's indirect cost claim. Trace all amounts to contractor's records.
- o If claimed actual rates are significantly higher than the contract ceiling rates, limit the review to verifying the contractor's computation of final indirect costs proposed and verifying the proposed amounts to the contractor's official records. However, any significant changes in the contractor's business and/or accounting practices must be fully investigated before a decision on limiting the review can be made.
- o Determine whether the accounting period used to allocate indirect costs is appropriate.
- o Review the organization structure, organization charts, and composition of the indirect cost pools to ascertain whether they are logical and bear a reasonable relationship to the bases used for allocating the indirect costs to operations.
- o Review and analyze specific indirect cost accounts to determine reasonableness, allowability, and allocability of the costs to Government contracts.
- o Examine miscellaneous income accounts and journal adjustments to ascertain their relationship to Government contract work.

- o Verify the accuracy of the allocation bases used to allocate the indirect cost pools to contracts, including the allocation of corporate home office to segments, where applicable.
- o Develop the indirect cost rates to be applied to each Government contract, following its terms and conditions.
- o Apply the indirect costs rates to the audited allocation bases incurred under each Government contract.

In addition, the following audit steps should be accomplished before the field audit is begun.

- o Review the contract to determine the basis established for determining the final allowable indirect cost rates. (DOE contracts generally provide for final rates to be based on negotiation rather than to be determined by audit.)
- o Review prior audit reports, workpapers, and the permanent audit file to understand the perceived reliability of the cost accounting system and related internal controls.
- o If not previously obtained, secure information about accounting changes that have occurred since the last audit of indirect cost pools.

F. DETAILED AUDIT OF INCURRED INDIRECT COSTS

The contractors should allocate indirect costs on a fiscal year basis.

1. Cost Accounting Period. The usual period for allocating indirect costs is the contractor's fiscal year. If there is a question about using the fiscal year, the guidance in CAS 406, Cost Accounting Period, is helpful, even if the contracts are not formally subject to the standard.

If, for some logical reason, a period of less than a year is used, determine whether accruals, deferrals, and other usual end-of-fiscal-year adjustments were properly made. An indirect cost rate should not be computed for a period longer than a year, unless the contractor changed its fiscal year.

2. Relationship of Indirect Cost Pools and Allocation Bases. Allocation bases must represent a reasonable measure of indirect cost.

a. General Concepts - Indirect costs should be allocated to contracts/final cost objectives using a base which best distributes the costs on a beneficial or causal relationship between the pooled costs and the contracts. Therefore, the base chosen must represent a reasonable measure of the indirect cost activity that is to be allocated. In this regard, a proper allocation base will vary in proportion to the related indirect costs, i.e., as the indirect costs increase, the base will increase, although not necessarily to the same degree. Once a proper base has been adopted, it should be followed consistently unless changed circumstances cause the previously accepted bases to allocate the indirect expenses inequitably. The auditor

should recognize significant changes such as the addition of indirect expenses which affect the homogeneity/content of the pooled costs, the mix of Government versus commercial work, etc.

b. Cost Accounting Standards Considerations - Where full CAS coverage is in effect, determine whether the indirect cost pools and allocation bases meet the requirements of CAS 418, Allocation of Direct and Indirect Costs, and CAS 410, Allocation of Business Unit General and Administrative Expenses to Final Cost Objectives. Where these CAS standards do not apply to the contract, the objective is still to determine whether each allocation base in use reasonably measures the benefits received or the casual relationship of the pooled indirect costs and the contract.

c. Allocation Base - For general and administrative expenses, a total cost input base most often represents the total activity of the business unit. (CAS 410 requires the use of a cost input base.) For overhead, CAS 418 asserts that a measure of resource consumption or output be used as a base unless the indirect cost pool contains a material amount of management or supervisory costs; then the base should represent the activity being managed or supervised.

d. Corporate Office General and Administrative - At multi-plant contractor locations, the general and administrative expenses generally include material amounts of corporate office administrative expense allocations. In such cases both the amounts allocated and the bases used by the home office to compute the allocations should be evaluated. Many times an audit of corporate office allocations has to be obtained through a request for an assist audit by the DCAA or another Government agency. If the contract(s) are subject to CAS, home office compliance with the requirements of CAS 403 has to be verified. Even when the contractor is not subject to the CAS, the requirements of CAS 403 regarding the hierarchy of allocation bases should be used as guidance. In this regard, keep in mind that the allocation base selected for residual expenses generally includes the total activities of all business segments.

Corporate office expenses are normally allocated to segments by (1) developing an overall corporate indirect expense rate, e.g., total allowable corporate expenses divided by total base costs of all segments, and (2) applying that rate to each individual segment's base costs.

e. Changing Allocation Methods - Present allocation methods are not necessarily rejected when they do not conform to the discussed criteria. Changes should be required (in the future) only if they result in materially different cost allocations. To demonstrate this effect, it may be necessary to reconstitute the indirect cost pools to obtain homogeneity and to use an acceptable base for allocating indirect costs. To aid in this activity, keep the following questions in mind when examining functional expense statements and individual accounts comprising each indirect cost pool.

- o Does the cost apply to all work represented by the allocation base?
- o Does the cost apply only to Government or commercial work?

- o If incurred only for Government work, does the cost apply to a specific contract or group of contracts?

Changes to contractors' overhead structures should be made prospectively. Also, the contractor should be formally advised of the required change as soon as possible or the Government may be estopped from disallowing cost in future years.

f. Preliminary and Final Assessments - Some preliminary conclusions on the acceptability of the indirect cost pools and bases may change following the detailed audit of indirect expenses and the verification of allocation bases. Reconsider preliminary conclusions after the detailed audit of indirect expenses and allocation bases is complete.

g. Cost Grouping - Except where segregated facilities that manufacture either commercial or Government products are maintained, contractors do not generally establish overhead structures that call for allocating indirect expenses based on separate Government and commercial allocation rates. Such a practice would generate an inordinate amount of administrative effort necessary to identify, record, and distribute indirect expenses by functions or duties performed. Indirect costs, by definition, are not readily identifiable by contract and/or customer. Any cost accounting system that allocates indirect expenses based on separate rates developed for commercial and Government work should be carefully examined to determine if the internal controls necessary to identify indirect costs accurately (particularly indirect labor) by customer have been established and are functioning properly.

The most appropriate method for allocating indirect expenses is the one which equitably measures costs allocable to all work. FAR 31.203(b), *Indirect Costs*, states

Indirect costs shall be accumulated by logical cost groupings with due consideration of the reasons for incurring such costs. Each grouping should be determined so as to permit distribution of the grouping on the basis of benefits accruing to the several cost objectives.

Under normal circumstances, separate Government and commercial expense pools are not necessary to meet these requirements.

Any significant indirect expense activity that does not meet the homogeneity test stated in CAS 418.50(b) can be removed from the expense pool and allocated on a different basis.

3. Selection of Individual Expense Accounts for Testing. Review account balances in each indirect cost pool allocated to Government contracts. Compare account balances with prior periods and with the current year's budget. Select accounts for detailed review and testing using the following criteria:

- o Significant amount,
- o Amount much larger than in prior years,

- o Costs do not conform to operational trends,
- o Account likely to contain unallowable costs, and
- o Costs are similar to costs charged direct to contracts.

4. Examination of Specific Expenses. The contract cost principles identify certain costs as expressly unallowable and place limitations on the reimbursement of other types of costs. The guidance presented below for items of cost deserving special attention should be applied in conjunction with the contract cost principles and written advance agreements when examining indirect cost accounts and testing transactions for reasonableness, allowability, and allocability.

Chapter 16 provides guidance for auditing various types of cost that are generally classified as Other Direct Charges. These same costs are sometimes treated as indirect expenses. Audit steps requisite to establishing the incurrence and reasonableness of the costs would not differ, irrespective of how the costs are classified. However, costs classified as indirect expenses should benefit the contractor's overall operations rather than one particular contract.

a. Screening Unallowable Costs - Ascertain whether the contractor has screened the following types of expressly unallowable expenses and has removed the costs from the total expense pool(s) allocated to Government contracts. The internal controls established to screen these expenses should be reviewed and a determination made as to whether they can be relied upon. If unallowable expenses were not screened or the internal controls established to screen them are not adequate, the audit must be expanded to cover this shortcoming. Also, the Contracting Officer must be so advised.

- o Advertising, except as specifically allowed in the contract cost principles.
- o Contingent expenses, or costs charged to indirect expense accounts which do not represent actual costs but merely a provision for costing.
- o Contributions.
- o Cost of organization or reorganization of an enterprise.
- o Entertainment.
- o Federal income taxes and other taxes specified in the contract cost principles as unallowable.
- o Facilities idle beyond 1 year or in excess of the time necessary to meet workload fluctuations.
- o Fines and penalties.
- o Interest, except that imputed through the cost of money calculation.

c. **Losses on other contracts.**

b. **Conference Costs** - When testing the allowability and reasonableness of conference costs, examine records supporting expense claims. Where questions arise, it may be necessary to examine individual diary records to understand the purpose of a conference and to establish that it was not entertainment.

c. **Computer Programming Costs** - Initial programming costs required to make a computer operational should be capitalized as part of the costs of the computer and the equipment installation costs. The costs should then be amortized over the anticipated useful life of the equipment.

d. **Depreciation** - The contract cost principles offer guidelines for determining the reasonableness of depreciation costs claimed in indirect expense pools. The cost allocation methods used require examination. If plant-wide depreciation rates are used, test them to determine whether more refined methods, based on departments or classes of equipment, would result in a material change in depreciation costs allocated to Government contracts.

For CAS covered contracts ascertain whether the requirements of CAS 404 and 409 are followed. FAR 31.205-11 should be reviewed before commencing an audit of depreciation costs.

e. **Independent Research and Development/Bid and Proposal Costs** - Independent Research and Development (IR&D) and Bid and Proposal (B&P) costs are required to be covered in an advance agreement. The auditor should determine the allowability and allocability of IR&D and B&P costs when advance agreements exist. If advance agreements are not required criteria specified in the FAR should be used to determine the allowability.

(1) **Advance Agreement.** The contract cost principles require that IR&D and B&P expense reimbursement be covered in an advance agreement when a contractor has received negotiated contracts or subcontracts exceeding an established threshold in the previous fiscal year (FAR 31.205-18). Where an advance agreement exists, determine the allowability and allocability of IR&D and B&P costs according to the terms of the agreement. If an advance agreement is required but has not been consummated, apply the criteria for reduction of payment specified in the contract cost principles (FAR 31.205-18(c)(1)(v)). For contractors who are not required to negotiate an advance agreement, allowability of IR&D and B&P costs should be determined according to the formula outlined in the contract cost principles (FAR 31.205-18(c)(2)).

(2) **Other Criteria.** The FAR requires that IR&D and B&P costs be accumulated by project and include all direct costs and allocable indirect costs, except general and administrative expense. If controls are adequate, the effort charged by technical or production personnel to overhead accounts should not relate to IR&D and B&P activities. However, these controls are sometimes circumvented when the IR&D-B&P cost ceiling has been exceeded. In other situations, management control over activities of technical and production personnel charging IR&D and B&P accounts during slack periods may be loose. FAR 31.205-18(b) incorporates all the requirements of CAS 420 for fully CAS covered contracts and cites two exceptions for modified CAS and

non-CAS covered contracts. The auditor should refer to this FAR subparagraph when auditing IR&D/B&P costs allocated to modified or non-CAS covered contracts.

(3) Test of Validity. Examine charges to indirect labor accounts to ascertain whether they contain costs of activities (such as concept formulation studies) that should be classified as IR&D and B&P effort. As another test of the validity of charges to the IR&D-B&P expense pool, examine project files, production records, and accounting records to determine whether any of the projects relate to production costs chargeable to contracts rather than to IR&D.

f. Indirect Material - Compare the costs of various categories of supplies with comparable expenditures for the prior year.

g. Insurance and Indemnification - Where significant insurance costs are charged to Government contracts, the contractor's insurance and indemnification program should be thoroughly examined periodically. Determine reasons for any marked increase.

Assure that the cost of self-insurance does not exceed the cost of obtaining equivalent coverage from an insurance company or State fund, considering comparable administrative costs. Actual loss experience should be reviewed to determine whether self-insurance charges for subsequent periods reflect past experience, as they would under a purchase plan. Where applicable, also determine whether the self-insurance program has been approved, as required by FAR 28.308(a).

If business interruption insurance is carried, assure that the premium excludes coverage for profit.

Assure that practices followed on CAS-covered contracts comply with CAS 416, Accounting for Insurance Costs.

h. Payroll Allowances, Fringe Benefits - Through tests, determine whether recorded payroll allowances conform to company policy and the contract cost principles. Examine justification to illustrate that fringe benefits are comparable with those of other firms in the industry.

i. Pension Costs - A detailed review of pension plan provisions and costs can be quite extensive. Where an independent audit has been made of the financial statements, it may be feasible to use work already done. In any event, FAR 31.205-6(j) incorporates the provisions of CAS 412 and 413. Therefore, when pension costs allocated to auditable contracts are significant, compliance with the CAS requirements must be verified.

j. Rental and Leasing of Facilities and ADP Equipment - The auditor should review leases to determine if the contractor complied with FAR requirements.

(1) ADP Leases. For ADP equipment rented under operating leases, review all necessary data to ascertain whether the contractor has complied with all the requirements of FAR 31.205-2.

(2) Other Leases. Review leases to determine what costs are to be paid by the lessee and whether any leases are classified as capital leases under FASB Statement No. 13, "Accounting for Leases". FAR 31.205-11(m) requires that assets acquired by capital leases must be treated as purchased assets. FAR 31.205-36 applies to operating leases, as defined in FASB Statement No. 13.

k. Selling Costs - Selling costs are subject to the same basic audit procedures and tests for allocability and reasonableness as administrative costs. However, there are certain factors for special consideration.

(1) Allocation. Selling costs should be apportioned to (1) product lines, classes of customers, or individual contracts according to the benefits derived by the particular cost objectives or (2) according to the purposes for which the expenses were incurred. As a general rule, selling costs are included in, and allocated with, general and administrative expenses. These costs are subject to a determination of allocability (See FAR 31.205-38).

(2) Reasonableness Test. Where selling costs are separated between commercial work and Government work, the reasonableness of selling costs related to Government work is a continuing concern if competitive constraints need not be exercised. In order to determine whether the costs are reasonable, compare ratios of selling expenses to contract or product sales volume for both commercial and Government work.

l. Special Facility Costs - Where special scientific facilities are used for a limited number of projects, assure that all readily identifiable direct costs are charged to users as incurred. Also ascertain whether general operating costs of a special facility are equitably allocated only to those projects which benefit from using the facilities. This determination could involve applying predetermined rates, based on elapsed time usage, and equitably distributing the variance between actual and applied costs.

m. Taxes - Care must be exercised regarding the propriety of allocation of certain taxes to Government work; for example, the allocation to all work of the contractor of personal property taxes levied against the contractor's commercial inventories may not be proper where similar taxes are not levied against Government contract inventories. State income or franchise taxes sometimes present unique allocation problems.

(1) State Taxes. State income or franchise taxes are normally collected and allocated as general and administrative expenses. However, for contractors doing business in several States, it is important to determine if the amount allocated to operations within a State is predicated on an allocation base representative of the factors on which the total payment is based. (See para. 403.40(b)(4) of CAS 403.)

When auditing claimed tax expenses the auditor should refer to FAR 31.205-41, particularly subparagraph (b)(6) regarding State income tax accruals representing differences between taxable income and pretax income being unallowable.

(2) Employment Taxes. For employment taxes, assure that liabilities are computed based only on the taxable wages of individuals.

n. Warranty Costs - The provisions of warranty clauses included in cost-reimbursable contracts differ considerably from those included in fixed price contracts. Cost-reimbursable contracts normally contain "Inspection and Correction of Defects" clauses which call for any costs related to correcting defects to be charged directly to the contract. Hence, any provision for warranty allocated to such contracts would result in double counting. When reviewing claimed warranty costs the auditor should (a) review the contract documents to determine the extent that warranty coverage differs by type of contract and (b) audit the incurred warranty costs to determine the contracts which generated the costs. If the costs pertained solely to fixed price or commercial orders, the provision would not be allocable to cost-reimbursable contracts.

5. Amortization of Prepaid Expense; Accrual of Liabilities. Test entries writing off prepayments or establishing liabilities for propriety, reasonableness, allocability to the accounting period, accuracy of computation, correctness of account distribution, and sufficiency of supporting documentation. The extent of verification depends on such factors as:

- o the acceptability of comparable testing done by the internal audit staff and the independent public accountant (for verifying published financial statements) and
- o the volume of costs being charged to Government contracts.

Review yearend adjusting journal entries to determine whether they affect contract costs. If so, determine that they were properly charged or credited to contracts or to indirect expense.

6. Miscellaneous Income and Credits. Review the nature of income received, other than from the sale of products or services. Ascertain whether any of the types of income in the accounts are actually reductions in incurred costs and whether the amounts were netted against costs claimed on Government contracts.

7. Verification of Indirect Cost Allocation Bases. After the propriety of the contractor's allocation bases has been established, it is necessary to verify that the proposed amounts of the bases include all the relevant activities. Simply stated, determine that all the activities that cause or benefit from the indirect expenses are included in the base. Establishing the accuracy of the base amount includes comparison and sometimes reconciliation to pertinent accounting and financial records such as certified financial statements, general ledger accounts, tax returns, labor distribution records, and job cost ledgers. Consider the following suggested audit procedures:

- o Verify that each activity base comprises all the costs or other units of measurement contemplated. Are all cost centers/departments in the organization assigned to an overhead center? Does the base include the activities of subsidiary companies, where appropriate?

- o Compare proposed bases with the preceding year to determine whether the elements or organizational units comprising each base are consistent with the prior year. Obtain reasons for any significant differences.
- o Determine whether costs excluded from indirect cost pools as not being allowable under Government work should be included in the applicable allocation base. This situation would occur when the unallowable or otherwise unallocable costs are of the same nature as the costs comprising the allocation base (See FAR 31.203(c).)

Having established the composition of each base for allocation of indirect costs, determine the correct base (or bases) for each Government contract. Assure that each Government contract base contains only the same elements that were used in the broad base verified above and that all applicable audit adjustments have been considered. For example, if direct labor dollars constitute the base for distribution of manufacturing overhead, assure that such items as shift pay, overtime compensation, overtime premium pay, off-site labor, or purchase labor are treated consistently in each Government contract allocation base compared to the overall allocation base for each indirect cost pool.

8. Development and Application of Indirect Cost Rates to Government Contracts. When the indirect cost pools have been audited and the activity bases for distribution have been accepted, develop the allocation rates. Distribute indirect costs to Government contracts by applying each audited rate to the appropriate contract activity base.

G. REPORTING

Separate reports are issued for separate audit assignments and when auditors are asked to comment on the appropriateness of entering into an advance agreement on certain costs to aid in negotiations.

1. Incurred Indirect Cost Audits. For larger contractors indirect costs are generally audited under a separate assignment, and a separate audit report is issued. Exhibit A (A:AM17EXA.WPF) contains the format for this report. In chapter 16 it was noted that, for small contractors, one audit report normally includes audit results of both direct and indirect cost audits (see chapter 16, exhibit A, A:AM16EXA.WPF).

When an audit report on indirect cost is issued, the ultimate impact of the audit adjustments on individual contracts cannot be established until the final overhead rates have been negotiated. Nevertheless, the allowable direct costs and any additional data related to the allocation bases (if other than direct costs) should be furnished to permit the contracting officer to determine the net effect of the potential disallowances on both individual and total contract costs.

2. Preward Audits. Refer to chapter 15 for the reporting requirements on preaward audits. Audit findings pertaining to the review of proposed indirect costs are discussed in exhibit B of that chapter (A:AM15EXB.WPF).

3. Advance Agreements. A separate report is generally issued when the auditor is asked to comment on the appropriateness of entering into an advance agreement on certain costs (FAR 31.109) to aid in negotiating reasonable indirect costs. No standard report form is specified, except it should be similar to reporting results of proposed (preaward) indirect cost, chapter 15, exhibit B (A:AM15EXB.WPF). The report should set forth the purpose, scope, results, and conclusion, according to the professional standards of audit reporting.

EXAMPLE OF INDIRECT COST AUDIT REPORT

OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITSAUDIT OF
INDIRECT COST RATES
CALENDAR YEAR 1988
ABC, INC.
CITY, STATE

REPORT NUMBER:

PURPOSE AND SCOPE

As requested by the Department of Energy (DOE), Field Office, Oak Ridge, we audited ABC, Inc.'s (ABC) indirect cost rates claimed for the calendar year ended December 31, 1988. ABC conducts energy research. Although most of its resources are dedicated to work for DOE, it performed some contract and grant work for other Federal agencies during the audit period.

The purposes of the audit were to determine the allowability, allocability and reasonableness of the indirect cost rates. Allowable costs are costs incurred that are reasonable, allocable, and in accordance with the terms of contracts, grants, applicable cost principles, laws and regulations, and generally accepted accounting principles and practices appropriate to the particular circumstances.

The audit scope was limited to reviewing the accounting books and records and other documents necessary to determine the allowability of claimed indirect costs and the reasonableness of costs comprising the allocation bases. In addition, we evaluated the appropriateness of the allocation methods used. We tested specific transactions, but did not evaluate ABC's total internal control system or technical aspects of its performance.

As defined in the above scope paragraph(s) we conducted our audit in accordance with generally accepted Government auditing standards that applied to this financial related audit. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the data and records reviewed are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records reviewed. An audit also includes assessing the accounting principles used and significant estimates made by the contractor, as well as evaluating the overall presentation. Criteria used in evaluating the claimed costs also included cost principles set forth in the Federal Acquisition Regulations (FAR), DOE Acquisition Regulations (DEAR), and the Cost Accounting Standards (CAS). We believe that our audit provides a reasonable basis for our audit conclusions.

We completed our onsite work on November 29, 1989.

CIRCUMSTANCES AFFECTING THE AUDIT

We did not perform a technical review of any contracts or grants. Accordingly, audit results are qualified pending the outcome of such technical reviews.

ABC's claimed indirect cost rates and the audit results are summarized below and detailed in exhibits A through D.

	Rate (Percentage)		
	<u>Claimed</u>	<u>Questioned</u>	<u>Per Audit</u>
Fringe benefit rate	26.9	(2.9)	29.8
Overhead rate	37.6	0.6	37.0
General and administrative rate	15.7	3.9	11.8
Overhead facilities capital cost of money factor	0.01845	0.01845	

We conclude that, except for the questioned rates summarized above and described in the notes to exhibit A, the indirect cost rates represent allowable indirect costs incurred in Calendar Year (CY) 1988.

Compliance with applicable laws and regulations related to the contracts and grants is the responsibility of ABC management. As part of our evaluation, we performed tests of compliance with certain provisions of laws and regulations related to the contracts and grants. Our objective was not, however, to reach a conclusion on overall compliance with such provisions.

Except for the matters described in the notes to exhibits A through D, the results of our tests indicate that, for the items tested, ABC complied in all material respects with the provisions of applicable laws and regulations related to the contracts and grants. For the items not tested, nothing came to our attention that caused us to believe that ABC had not complied, in all material respects, with those provisions.

We discussed the audit results with ABC's controller on November 29, 1989.

OTHER MATTERS TO BE REPORTED

In planning and performing our audit of indirect cost rates claimed by ABC for CY 1988, we considered ABC's internal control structure to determine our auditing procedures for the purpose of reaching a conclusion on these indirect cost rates and not to provide assurance on the internal control structure.

ABC management is responsible for establishing and maintaining an internal control structure that will ensure costs claimed are allowable under the contract. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure regarding allowable costs are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit preparation of indirect cost rates in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purposes of this report we classified the significant internal control structure policies and procedures as those that relate to the recording and reporting of costs under Government contracts and grants and to ensuring compliance with laws and regulations that have a material impact on indirect cost rates claimed. These are control procedures designed to ensure that:

- o The breakdown of costs within the accounting system was adequate for cost determination purposes.
- o Specific cost elements were afforded consistent treatment regarding Government and non-Government cost objectives.
- o Allowable and unallowable costs were routinely identified and segregated in the accounting system.
- o Adequate source documentation supported all costs.
- o Assets were safeguarded against loss or unauthorized use or disposition.
- o All accounting data were accurate, reliable, and traceable to underlying source documentation.
- o Applicable laws and regulations were known by appropriate personnel, and the effects of laws and regulations were properly reflected in the accounting records.

For the internal control categories listed above, we obtained an understanding of the design of relevant policies and procedures, determined if they have been placed in operation and assessed control risk.

We noted a certain matter involving the internal control structure and its operation that we consider a reportable condition under standards established by the American Institute of Certified Public Accountants. Reportable conditions are matters coming to our attention relating to significant deficiencies in the internal control structure design or opera-

tion that, in our judgment, could adversely affect ABC's ability to record, process, summarize, and report financial data for indirect costs consistent with management's assertions. This reportable condition is that the accounting system does not identify and segregate unallowable costs.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to indirect cost rates being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control structure would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. We conclude that the condition described above is a material weakness.

RECOMMENDATION

We recommend that DOE direct ABC to establish an adequate chart of accounts that identifies and segregates allowable and unallowable costs.

CONTRACTOR'S COMMENTS

ABC's controller concurred with the audit results.

JOHN DOE & COMPANY

By: _____

ACCEPTED BY:

INSPECTOR GENERAL

OFFICE OF

Exhibit A
Page 1 of 2

ABC, Inc.
City, State

Claimed Fringe Benefit Rate and Audit Results
Calendar Year 1988

<u>Expense</u>	<u>Claimed Costs</u>	<u>Audit Results</u>	
		<u>Questioned Costs</u>	<u>Notes</u>
Federal Insurance Con- tribution Act (FICA)	\$ 84,000		
Unemployment Taxes	2,000		
Health Insurance	40,000		
Life Insurance	6,000		
Pension	74,000		
Vacation	62,000		
Holiday	35,000		
Sick	18,000		
Workers Compensation	<u>2,000</u>		
Total	<u>\$ 323,000</u>		
<u>Allocation Base</u>			
Total Labor	<u>\$1,200,000</u>	<u>\$115,000</u>	1
Fringe Benefit Rate	<u>26.9 percent</u>	<u>(2.9) percent</u>	
Rate per Audit	<u>29.8 percent</u>		2

NOTE: The figure in parentheses is an increase.

REPORT NUMBER:
NOTES TO EXHIBIT A

Exhibit A
Page 2 of 2

1. ABC erroneously included vacation, holiday, and sick pay in both the numerator and denominator of its fringe benefit rate. Because ABC recovers vacation, holiday, and sick pay through application of its fringe benefit rate, we decreased the base to exclude these costs.
2. We calculated the fringe benefit rate per audit as follows:

Fringe benefits	<u>\$ 323,000</u>
Labor (\$1,200,000 minus \$115,000)	<u>\$1,085,000</u>
Rate (\$323,000 divided by \$1,085,000)	<u>29.8</u> pct.

REPORT NUMBER:

Exhibit B
Page 1 Of 2ABC, Inc.
City, StateClaimed Overhead Rate and Audit Results
Calendar Year 1988

<u>Expense</u>	<u>Claimed Costs</u>	<u>Audit Results</u>	
		<u>Questioned Costs</u>	<u>Notes</u>
Overhead Labor	\$ 60,000		
Fringe Benefits	16,140	\$(1,740)	1
Supplies	40,000		
Reproduction and Printing	25,000	6,000	2
Telephone	25,000	1,200	3
Insurance	15,000		
Rent	100,000		
Maintenance and Repairs	20,000		
Postage	3,600		
State and Local Taxes	500	500	4
Depreciation	50,000		
Other	<u>250</u>	<u> </u>	
Total	<u>\$355,490</u>	<u>\$ 5,960</u>	

Allocation Base

Direct and B&P Labor	<u>\$945,000</u>		
Overhead Rate	<u>37.6 percent</u>	<u>0.6 percent</u>	
Rate per Audit	<u>37.0 percent</u>		5

NOTE: The figure in parentheses is an increase.

REPORT NUMBER:
NOTES TO EXHIBIT BExhibit B
Page 2 of 2

1. We calculated questioned fringe benefit costs as follows:

Difference between claimed 26.9 percent fringe benefit rate and the 29.8 percent rate per audit applied to overhead labor costs [(2.9) percent x \$60,000]	\$(1,740)
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2. Costs claimed included \$6,000 of direct printing costs for a commercial client. We questioned these costs because they are direct costs according to FAR 31.202(a), Direct Costs.
3. ABC did not reduce telephone costs by \$1,200 refunded by employees for personal phone calls. Such refunds represent credits that should be offset against telephone costs in accordance with FAR 31.201-5, Credits.
4. ABC claimed state corporate income taxes of \$500. This is a G&A expense, as defined in FAR 31.001, Definitions, because it is necessary for ABC's general administration. We questioned this amount in accordance with FAR 31.203(b), Indirect Costs.
5. We calculated the overhead rate per audit as follows:

Overhead costs (\$355,490 minus \$5,960)	\$349,530
Direct and B&P labor	\$945,000
Rate (\$349,530 divided by \$945,000)	37 pct.

REPORT NUMBER:

Exhibit C
Page 1 of 4ABC, Inc.
City, StateClaimed
General and Administrative Rate and Audit Results
Calendar Year 1988

Expense	Claimed Costs	Audit Results	
		Questioned Costs	Notes
G&A Labor	\$ 80,000		
B&P Labor	50,000		
Fringe Benefits	34,970	\$(3,770)	1
B&P Overhead	18,800	300	2
B&P Over Ceiling		39,000	3
Consultants	27,000	20,000	4
Employee Relocation	11,800	1,800	5
Legal and Accounting	22,000	1,200	6
Licenses and Fees	800		
Insurance	30,000		
Advertising	7,500	1,200	7
State and Local Taxes	3,200	1,200	8
Penalties and Interest	150	150	9
Contributions	1,850	1,850	10
Employee Morale	300		
Amortization	1,000	200	11
Travel	5,550	2,050	12
Miscellaneous	<u>10,800</u>	<u>10,000</u>	13
Total	<u>\$ 305,720</u>	<u>\$75,180</u>	

Allocation Base

Total Costs Excluding G&A	<u>\$1,953,580</u>	<u>\$(6,030)</u>	14
G&A Rate	<u>15.7 percent</u>	<u>3.9 percent</u>	
Rate per Audit	<u>11.8 percent</u>		15

NOTE: The figures in parentheses are increases.

REPORT NUMBER:
NOTES TO EXHIBIT CExhibit C
Page 2 of 4

1. We calculated questioned fringe benefit costs as follows:

Difference between claimed 26.9 percent
fringe benefit rate and the 29.8 percent
rate per audit applied to G&A and B&P
labor [(2.9) percent x \$130,000] \$(3,770)

2. We calculated questioned B&P overhead costs as follows:

Difference between claimed 37.6 percent
overhead rate and the 37 percent rate per
audit applied to B&P labor (0.6% x \$50,000)\$ 300

3. Bid and proposal costs exceeded amounts allowable per FAR 31.205-18(c)(2), Independent Research and Development and Bid and Proposal Costs. Questioned costs represent the difference between costs claimed and the ceiling computed in accordance with FAR 31.205-18.
4. Consultant costs claimed included \$20,000 paid to a marketing consultant. Because costs were not supported by a contract, we could not determine the allowability in accordance with FAR 21.305-33(b)(8). Through discussions with the president and a review of the invoice, we noted that ABC placed two telephone calls to the U.S. Small Business Administration and hosted a sailing escapade on the Potomac River to entertain lobbyists. We also questioned these costs in accordance with FAR 31.205-14, Entertainment Costs, and FAR 31.205-50, Executive Lobbying Costs.
5. Costs claimed include \$1,800 for relocation costs for a new employee who resigned within 6 months after relocating. We questioned these costs in accordance with FAR 31.205-35(d), Relocation Costs.
6. Costs claimed include \$1,200 for legal services related to obtaining a patent on a new invention that ABC plans to market commercially next year. We questioned these costs in accordance with FAR 31.205-30(c), Patent Costs, because they were not related to a Government contract and because ABC maintains the patent's title.
7. We calculated questioned advertising costs of \$1,200 as follows:
- a. Costs claimed included \$1,000 for a television advertisement testimonial about ABC's extraordinary services. We questioned these costs as unallowable in accordance with FAR 31.205-1(f)(5), Public Relations and Advertising Costs.
 - b. Costs claimed included \$200 for a booth at a trade show for displaying the new invention (Note 6). We questioned these costs as unallowable in accordance with FAR 31.205-1(f)(2)(i).

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NOTES TO EXHIBIT CExhibit C
Page 3 of 4

8. We calculated questioned state and local taxes of \$1,200 as follows:
- a. Costs claimed included \$1,700 for Federal income taxes. We questioned these costs as unallowable in accordance with FAR 31.205-41(b)(1), Taxes.
 - b. We questioned \$(500) reclassified from overhead as discussed in Exhibit B, Note 4.
9. We calculated questioned penalties and interest of \$150 as follows:
- a. Costs claimed included \$40 for two parking tickets for the president's car. We questioned these costs as unallowable in accordance with FAR 31.205-15, Fines and Penalties.
 - b. Costs claimed included \$110 for penalty and interest for late filing of ABC's tax return. We questioned these costs as unallowable in accordance with FAR 31.205-15, and FAR 31.205-20, Interest and Other Financial Costs.
10. ABC claimed \$1,850 for contributions. We questioned these costs in accordance with FAR 31.205-8, Contributions or Donations.
11. Amortization costs included \$200 for organization costs. We questioned these costs in accordance with FAR 31.205-27(a), Organization Costs.
12. We calculated questioned travel costs of \$2,050 as follows:
- a. Costs claimed included \$2,000 for a ski trip to Vail with ABC clients and spouses. We questioned these costs as unallowable in accordance with FAR 31.205-14, Entertainment Costs, and FAR 31.205-46(b), Travel, because they were not necessary for the overall administration of the business.
 - b. Costs claimed included \$50 for the purchase of alcoholic beverages. We questioned these costs as unallowable in accordance with FAR 31.205-51, Costs of Alcoholic Beverages.
13. ABC claimed \$10,000 for a loss on a firm-fixed-price contract. We questioned this cost, because it is unallowable under FAR 31.205-23, Losses on Other Contracts.
14. We calculated questioned G&A base costs of \$(6,030) as follows:
- a. We questioned \$3,770 of fringe benefits reclassified as G&A per Note 1, above.
 - b. We questioned \$(300) of B&P overhead per Note 2, above.

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NOTES TO EXHIBIT CExhibit C
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- c. We questioned \$500 of costs reclassified as G&A per Note 8.b., above.
 - d. We questioned \$(10,000) corresponding with the loss on the fixed-price contract discussed in Note 13, above.
15. We calculated the G&A rate per audit as follows:

G&A expense (\$305,720 minus \$75,180)	\$ 230,540
Total costs excluding G&A (\$1,953,580 plus \$6,030)	\$1,959,610
Rate (\$230,540 divided by \$1,959,610)	11.8 pct.

A:AM17EXA.WPF

EXHIBIT A

REPORT NUMBER:

Exhibit D

ABC, Inc.
City, State

Claimed
Overhead Facilities Capital Cost of Money Factor
Calendar Year 1988

	<u>Proposed Costs/Rates*</u>
Applicable Cost of Money Rate	9.47 pct.
Average Net Book Value	<u>\$184,076</u>
Cost of Money	<u>\$17,432</u>
Allocation Base	<u>\$945,000</u>
Overhead FCCM Factor	<u>0.01845</u>

* We take no exception to these costs and rates.

CHAPTER 18REVIEW OF COST ACCOUNTING SYSTEMSA. SCOPE OF CHAPTER

This chapter applies to any audit or review of a present or prospective contractor's or subcontractor's cost accounting system. The review may be made in conjunction with a preaward audit of a pricing proposal or an audit of incurred costs on an existing contract, or it may be undertaken as a separate audit. One purpose of a separate audit may be to determine compliance with applicable CAS and FAR requirements.

B. OBJECTIVES OF AN AUDIT OF A COST ACCOUNTING SYSTEM

The primary objective of a cost accounting system audit is to determine if the accounting system is adequate for controlling, segregating, accumulating, and reporting costs under a Government contract. The financial and compliance elements of contract auditing are emphasized.

The cost accounting system may also be reviewed to judge whether existing practices produce reasonable costs in cases where a firm may not be subject to competitive restraint. As a corollary, the review may also explore whether existing practices can be made significantly more efficient or economical.

The cost accounting system may also be reviewed to determine its compliance with relevant CAS requirements. See exhibit A (A:AM18EXA.WPF) for a listing of the CAS standards. Where a CAS disclosure statement is required, the statement is generally reviewed separately for adequacy.

C. REVIEW OF INTERNAL ACCOUNTING CONTROLS

A contractor's internal controls should be reviewed to determine whether they are adequate to assure that cost representations related to Government work are accurate and whether they conform to Federal laws, regulations, and contract provisions. Also, the extent of reliance that can be placed on the internal controls generally determines the intensity of future audit effort. In this regard, the number of tests made of evidential matter, the number of observations made of the contractor's operations, etc., normally correspond inversely to the degree of reliance placed on the internal controls.

A special review designed specifically to evaluate a contractor's internal control system as a whole should not be undertaken unless requested by contracting officials. With the exception of contractor locations having a continuing, very heavy volume of Government work, performance of these reviews would not be cost effective. Hence, audit reports should normally contain a disclaimer in the scope paragraph, indicating that a comprehensive audit or review of the total internal control system was not made. However, since the review of internal controls is an integral part of any audit, the system should be examined to the extent considered necessary to accomplish the audit objectives, and any weaknesses uncovered should be reported on an exception

basis. The guidance furnished in the subsequent paragraphs should be used selectively, based on the scope needed to meet the audit objectives of individual assignment.

1. Development of Evidence. The review is made through various means, including physical examination, observation, interview, examination of organization charts, flow charts, procedures manuals, and accounting records and reports.

2. Scope of Initial Review. The depth of the scope of the initial review of internal controls will generally depend on two factors: (1) the extent of Government participation in the total operation, including the types of contracts involved, and (2) whether others previously reviewed the internal controls, i.e., independent public accountants and/or internal auditors. If others reviewed the internal controls, the auditor then must be assured that the review was adequately accomplished and that any conclusions reached are sound. However, caution should be exercised when relying on the work of others, as explained below.

a. Use of an Independent Auditor's Work - Field work auditing standards require an independent auditor to obtain a sufficient understanding of the internal control structure to plan the audit and determine the nature and extent of tests to be performed. This understanding covers internal accounting controls that relate to the reliability of financial records and to the safeguarding of assets, as both apply to published financial statements. The purpose of the independent auditor's study is to determine the extent of testing necessary to form an opinion on the financial statements.

Clearly, the independent auditor's objectives are different from the type of review of internal accounting controls contemplated under this chapter. Nevertheless, the independent auditor's work is complementary to that done under these guidelines and should be reviewed and used to the extent feasible. For example, as part of the examination of the financial records' reliability the independent auditor seeks to develop assurance that all transactions applying to a given fiscal period have been recorded correctly. This verification is equally important to any review made under the guidelines of this chapter. The review made by the independent auditor of the verification and safeguarding of assets and the division of responsibilities regarding the use of assets is also valuable. Since most assets generate expected costs over time (which are generally allocable to Government work), a review of the internal accounting controls must also be concerned with the control of assets.

b. Use of Internal Audit Work - A competent internal audit staff, which advises management whether or not policies are being effectively implemented, provides additional internal control. The internal audit staff's effectiveness as an element of internal control will depend on: (1) management's motivation for its establishment, (2) the extent of its independence from internal influences, (3) the extent of responsibility and delegated authority, (4) its status in the organization, and (5) the official to whom the internal audit group reports.

At contractor locations where DOE work is continuous and a competent internal audit staff exists, it may be feasible to coordinate the audit

program in areas of mutual interest, providing the internal audit staff's effectiveness has been established according to the above criteria. Reliance on work performed by the internal audit staff should be based on a review of the audit program and working papers, not just the audit report. This reliance may enable the auditor responsible for internal control evaluations to curtail his work.

3. Audit Effort Applying to Government Contracts. Inadequate accounting controls can affect costs on Government contracts. To assure that recorded contract costs are reasonable, allowable, and properly allocable, one needs to go beyond the usual internal control coverage of independent auditors or internal auditors. Certain basic questions need to be posed and answered to assure that the Government's interests are protected.

- o Adequacy of Cost Account Breakdown for Government Work - Is the breakdown of cost accounts adequate for both cost determination and cost estimation under Government contract cost principles and practices?
- o Proper Classification and Assignment of Costs - Are there any factors which could cause transactions to be classified improperly in violation of stated procedures and practices?
- o Avoiding Distortion of Results from Double Counting - Where the requirement for resources varies significantly between jobs in a single cost collection center, what assurance exists that "double counting" of costs incurred for the same purpose does not occur?

Each question is developed in turn in the sections that follow.

a. Adequacy of Cost Account Breakdown for Government Work - Determine whether costs which are declared unallowable (FAR 31.205) are segregated and accumulated in separate accounts. If this segregation is not established policy, determine how the firm deems its cost accounting system suitable for cost estimation and cost determination consistent with the FAR.

b. Proper Classification and Assignment of Costs - Proper classification of costs is an essential requirement for an acceptable accounting system, both for Government contract costing purposes and financial accounting. Costs need to be classified to develop cost data useful to management for (1) reporting the results of operations, (2) budget planning, (3) controlling costs through responsibility accounting, (4) establishing a pricing policy, and (5) accumulating and analyzing product costs.

Costs are normally grouped into various classifications, according to management's needs. The classifications that are most significant to Government contract costing follow.

(1) Nature of the Costs. Costs should be properly segregated by main groupings such as direct materials, direct labor, indirect expenses, and appropriate subgroupings as considered necessary. Indirect expenses should be further identified by expense categories such as advertising, rent, entertainment, etc. All these cost elements should be listed and adequately defined in a chart of accounts.

(2) Cost Centers. Grouping of costs by cost centers permits the flow of costs to be identified directly to individuals responsible and accountable for its incurrence. It also facilitates developing indirect expense rates for allocating indirect costs.

(3) Contract. Segregating costs by contract is essential to having an adequate cost accounting system for contract costing purposes.

Attribute testing of transactions can be used to determine whether costs have been assigned to the proper accounts and contracts. But attribute testing will not necessarily reveal internal control weaknesses caused by factors which influence the classification of transactions by individuals. Constraints which may cause a departure from accepted accounting practices include: (1) cost limitations or ceilings in organizational budgets or contracts, (2) material usage standards, and (3) labor efficiency standards.

Supplemental testing can be done with job history information. Review job history records and list jobs facing potential overruns or unfavorable variances from established standards. This record becomes the audit target list to be used in connection with review of the accounting for labor and material costs described below.

(a) Accounting for Labor Costs - Use the following steps as a guide for reviewing labor cost accounting.

- o Review labor distribution records for several periods. Investigate cases where individuals who are normally carried as direct labor have charged considerable time to indirect expense. Ascertain whether these individuals previously charged time to the jobs on the audit target list. If so, examine available evidential matter to confirm that they did indeed work on indirect projects.
- o If a standard cost accounting system is being used, review the basis for developing the standards and check whether they are updated periodically. Also, confirm that the type of labor effort being charged directly to the contract is consistent with that considered in developing the direct labor standards.
- o Review the established timekeeping procedures to the extent necessary to satisfy yourself that they result in a proper identification of labor costs. Determine whether the entries and any corrections on the time cards were made by the employee and whether they were properly approved. Also review the adequacy of procedures related to subsequent adjustments of contract costs, i.e., transfers between contracts or from contracts to indirect expenses. In this regard, a number of cases have surfaced where costs have been transferred from contracts that are overrun to other contracts and to indirect expense. Such transfers should be adequately documented and properly approved by higher management officials. Also, the transfers should be made through "nonstandard" journal entries; they should not be intermingled with the normal, monthly transactions.

(b) Accounting for Material Costs - Use the following steps as a guide for reviewing material cost accounting.

- o Determine whether there is accountability of material issued to each job or work order. Are material withdrawals from stores, and are purchases charged direct to contracts adequately documented and approved?
- o Determine if the disposition of all items not used on a particular job (i.e., returns to stock, spoilage, or scrap can be accounted for and whether the accounting treatment is consistent. Are Government-owned materials properly identified and segregated from other material items?
- o If Government-owned facilities are used in the production process, are they being utilized in accordance with contractual provisions? Are they properly identified and is their usage adequately documented?
- o Does the contractor solicit competitive bids whenever possible? Review procurements of selected major components to establish whether they were awarded on a competitive basis. Are assignments for purchasing specific types of items

(c) Accounting for Costs Other Than Labor and Material - Costs classified as other than direct labor and direct materials should be treated consistently. These costs are normally classified as "Other Direct" and "Indirect Expenses." Auditors should review contractor practices regarding criteria for determining how costs are charged to Government contracts. If the contractor must submit a disclosure statement, much of this information is furnished in the Statement, Form CASBDS-1. If a disclosure statement has not been submitted, the contractor should be asked to provide the same information concerning the accounting treatment of costs as is requested by the disclosure statement. Special attention should be devoted to costs which may be treated both as direct and indirect, such as fringe benefits, overtime and shift premium, freight out, warranty, travel, incoming inspection, engineering, and special tooling and test equipment. Contractors also treat the cost of purchased labor differently. Some classify it as "Other Direct Cost" while others treat it as direct labor and include it in the overhead allocation base. The most pertinent point to remember, as far as consistency in accounting for costs is concerned, is that costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives, as stated in CAS 402, "Consistency in Allocating Costs Incurred for the Same Purpose." The requirements of this standard apply to all contractors, irrespective of whether they have CAS covered contracts.

c. Avoiding Distortion of Results from Double Counting - In the previous paragraph, CAS 402 was cited as the standard that directly addresses the requirement for treating each type of cost consistently. The fundamental purpose of this standard is to make sure that such costs are allocated only once and on only one basis to any contract. Double counting occurs when the same type of cost is charged to a contract both as a direct charge and as an

overhead allocation. For example, a contract administrator, assigned to a single, very large program, charges his salary directly to the contract. At the same time, other contract administrators who are assigned two or more contracts charge their salaries to indirect expense. The large program is being overcharged, because it is being charged twice with the same type costs under like circumstances. Double counting frequently occurs when executives (usually those in smaller firms) charge their efforts both direct to contracts and to G&A expenses. If the executives' time is properly segregated between contract and administrative effort, no double counting occurs, because the costs are not incurred under "like circumstances." Hence, the auditor must assure himself that adequate timekeeping procedures are in effect and that they are consistently followed.

D. REVIEW OF THE COST ACCOUNTING AND MANAGEMENT SYSTEMS FROM THE STANDPOINT OF EFFICIENCY AND ECONOMY

The audit guidance furnished to this point has been directed mainly toward verifying whether a contractor's accounting system is adequate to properly accumulate the actual costs incurred in performing Government work. Actual costs incurred, however, may not be reasonable if they result from inefficient and wasteful management practices. Performance audits or functional reviews have been developed to evaluate major areas of contractors' operations with the objective of uncovering, reporting, and correcting wasteful or inefficient operations in order to reduce future costs of Government contracts.

Since the proper planning and accomplishment of a comprehensive performance audit program requires a considerable amount of audit effort, these audits are generally accomplished only at contractor locations with a very heavy volume of auditable work, such as where a resident audit staff is assigned. For this reason, extensive audit coverage on this subject is not warranted. Guidance will be restricted to a discussion of cost accounting as an aid in cost control and the selection and identification of some major areas where operations audits are normally accomplished.

1. Cost Accounting as an Aid in Cost Control. Contractors that are conscientious about maintaining efficient and economical operations will design and use the cost accounting system to help control costs. Cost accounting systems help control costs when the costs are identified with persons having some responsibility for their control. Determine whether costs are categorized according to responsibility centers. Establish whether cost performance reports are issued for each level of responsibility following established lines of authority and whether the reports delineate the costs considered controllable at each level. Determine whether managers of responsibility centers are held accountable for controlling costs within budgeted amounts or other performance standards.

(a) Indirect costs tend to become fixed over time. Determine if the need for the existing capacity of each activity generating indirect costs is periodically reviewed. Also determine whether indirect costs are controlled at the point of cost incurrence rather than at the various levels to which such costs are allocated.

(b) If responsibility accounting, as described above, is not used, determine if cost reporting and control are exercised over major cost categories of both direct and indirect costs. Ascertain whether the process is effective.

(c) For support and service centers, ascertain if cost reports clearly illustrate whether the recipient departments have used the services at planned levels. Also, determine if the cost allocations are based on reasonable measures of causal or beneficial relationships and if the services rendered are adequately documented.

2. Selecting Functional Areas for Review. A properly planned comprehensive program for accomplishing performance audits begins with a thorough analysis of the contractor's organization and the functions performed by each department/cost center. Published management policies and procedures should also be thoroughly analyzed and evaluated. The knowledge gained through these analyses, coupled with the results of incurred cost audits, preaward audits, and accounting system and internal control examinations, should be sufficient for the auditor to identify weak areas that need to be reviewed. Typical areas selected for an performance audit are purchasing and subcontracting, estimating practices, production and control, budgeting practices, and labor recording and utilization practices.

E. NEED FOR PERIODIC REVIEW AND UPDATING OF PERMANENT FILE

The workpapers of accounting systems reviews should be made part of the permanent audit file. They represent valuable reference material for subsequent audits of pricing proposals or incurred costs. The permanent audit file should be updated each time a preaward or cost-incurred audit is made.

Several factors could diminish the reliability of the internal accounting controls. Organizational changes and personnel changes often can affect the reliability of controls. Changes in the mix of business can have a similar effect. Consequently, where there is a significant amount of continuing Government business, the cost accounting system and the underlying internal accounting controls should be reviewed periodically as major changes occur.

F. COST ACCOUNTING STANDARDS REVIEW

Contracts and subcontracts subject to the CAS requirements will contain the clauses prescribed by the procurement regulations. There are two types of coverage, full and modified. Modified CAS coverage requires compliance with Standard 401, "Consistency in Estimating, Accumulating and Reporting Cost," and Standard 402, "Consistency in Allocating Costs Incurred for the Same Purpose." Reports on CAS reviews should indicate the type of coverage in effect.

Where full coverage applies, the auditor is responsible for determining whether a contractor's

- o disclosure statement, submitted as a condition of contracting, adequately describes the actual or proposed cost accounting practices as required by Public Law 91-379;

- o disclosed cost accounting practices comply with contract cost principles and applicable cost accounting standards;
- o failure to comply with applicable cost accounting standards or to follow consistently its disclosed cost accounting practices has resulted, or may result, in increased cost to the Government; and
- o proposed price changes, submitted as a result of changes made to previously disclosed or established cost accounting practices, are fair and reasonable; and the appropriate CAS clause was included in subcontracts, where required, and that such covered subcontracts are adequately administered and audited.

1. Review of Disclosure Statement for Accuracy. The auditor should review the disclosure statement to ascertain if it adequately describes the cost accounting practices to be used by a contractor for estimating, accumulating and reporting contract costs.

a. Description of Adequacy - To be considered adequate, a disclosure statement must be current, accurate, and complete. A disclosure statement is current if it describes the cost accounting practices which the contractor intends to follow for estimating, accumulating, and reporting costs associated with covered contracts. The disclosure statement, therefore, could possibly include practices that are currently in use; will be instituted at some future date; will be followed with the incurrence of a new cost; or a combination of these.

Existing audit files should be reviewed to ascertain whether the cost accounting practices identified in the disclosure statement are, in fact, the contractor's current practices. For example, data in the permanent file and in recent reports on pricing proposals, indirect cost rate proposals, and accounting system surveys cover many features of the contractor's cost accounting practices. When the adequacy review discloses a difference between a described practice and an existing practice, discuss it with the contractor to learn if a change in practice is intended. Conversely, if an intended change in the contractor's practice has not been described, the audit report should recommend that the contractor describe the intended practice as well as the existing practice.

Where the contractor already has covered contracts, but was not previously required to file a disclosure statement, the practices subsequently described should be the same as those used to estimate and accumulate costs for the contracts entered into before the disclosure statement was required. If there are any known differences, a review should be scheduled to ascertain if the contractor is consistently following established cost accounting practices that were effective when the initial covered contract was awarded.

A disclosure statement is accurate if it correctly, clearly, and distinctly describes the actual method of accounting the contractor or subcontractor uses or intends to use on contracts subject to Public Law 91-379. Vague, ambiguous, and contradictory descriptions of the contractor's cost accounting practices may hinder subsequent compliance reviews, cause disputes and litigation between contracting parties, and ultimately cost the

Government more. Carefully review the described practices for specificity and clarity. Clerical accuracy is also a requirement for the disclosure statement. Verify whether the contractor has checked the appropriate boxes, inserted the applicable code letters, omitted any questions, etc.

The interrelationships of various sections of the disclosure statement are listed in exhibit B (A:AM18EXB.WPF) to facilitate the review for accuracy.

b. Materiality - Materiality should be a major factor in determining the level of detail required to be disclosed. A prime consideration should be whether a change in accounting procedure at the level of detail under consideration would materially affect the flow of costs, now or in the near future.

c. Audit Workpapers - Refer to chapter 7 of this Manual for guidance on the preparation of workpaper support. Contract audit workpapers should contain, as a minimum, (a) the basis for considering the described practices acceptable, (b) a record of discussions and written communications with the contracting official and contractor, and (c) the auditor's rationale in resolving questionable items. The workpapers should identify those descriptions accepted without audit verification. This identification is especially important for those described practices which involve significant costs. In this way, the auditor will have a basis for identifying these practices and reviewing such items for compliance when future audits are performed

d. Reporting - Reports on the adequacy of disclosure statements should be submitted separately from other reports concerned with pricing proposals or noncompliance matters. The format is shown as exhibit C (A:AM18EXC.WPF). Exhibit D (A:AM18EXD.WPF) shows the format for an accounting system review.

2. Compliance Reviews. The purpose of the compliance review is to ascertain whether the disclosed or established practices comply with both the CASB rules, regulations, and standards and with the FAR contract cost principles and procedures.

a. Types of Noncompliance - Eight types of noncompliance (enumerated below) can be identified based on CASB rules, regulations, and standards and the contract cost principles.

- o Disclosed practices do not comply with CAS.
- o Disclosed practices do not comply with contract cost principles.
- o Actual practices of estimating costs do not comply with CAS.
- o Actual practices of estimating costs do not comply with contract cost principles.
- o Actual practices of estimating costs do not comply with the disclosure statement.

- o Actual practices of accumulating or reporting costs do not comply with CAS.
- o Actual practices of accumulating or reporting costs do not comply with the contract cost principles.
- o Actual practices of accumulating or reporting costs do not comply with the disclosure statement.

The first two noncompliance situations may be detected either during the initial disclosure statement review, during regular audits such as price proposal evaluations, or during incurred cost audits. The next three conditions would likely be detected during a proposal evaluation or an estimating system survey. The final three situations would generally be detected during regular or routine audits of actual costs.

b. Review of Disclosure Statement for Compliance with CAS - The initial review of a disclosure statement for CAS compliance may be made concurrently with the adequacy review discussed in the preceding section. However, the report on adequacy of the disclosure statement should not be deferred pending completion of the compliance review. Exhibit E (A:AM18EXE.WPF) contains detailed guidance for conducting this compliance review.

c. Review of Actual Practices for Compliance with CAS - Where disclosure statements are not required but the contract stipulates CAS coverage (either full or modified), compliance reviews of actual practices may be made as a separate assignment. CAS compliance would always be a consideration in pricing proposal evaluations and in incurred cost audits. Exhibit E (A:AM18EXE.WPF) contains detailed guidance for making compliance audits.

3. Cost Impact Proposals. This section contains guidance applicable to the review of cost impact proposals which are submitted in accordance with the price adjustment provisions of the CAS clause. The CAS clause requires the prices of CAS covered contracts to be adjusted when noncompliance increases costs to the Government. The clause also requires equitable adjustments to CAS covered contracts when a new standard causes a change to be made in contractors' accounting practices and when the Contracting Officer and the contractor agree on a change to a disclosed or established practice. Remember that contract price adjustments are made only if the net increase or decrease is material. The vehicle for determining the cost impact of the noncompliance and for conducting negotiations to reach agreement on price adjustments is the cost impact proposal, prepared by the contractor and reviewed by the auditor.

When a contractor is in noncompliance with CAS requirements and the cost difference is believed to be material, audit involvement will take one of two forms.

a. Cost Impact Proposal Not Submitted by Contractor - If the contractor fails to submit a cost impact proposal, the contracting official will request an audit to develop an estimate of the cost impact. The objective is to provide sufficient information for the contracting official to make a unilateral decision. This procedure would shift the burden of proof to

the contractor, since the contractor would have to rebut the Government's position.

The audit report should include the scope of the review, a description of the circumstances relating to the contractor's failure to submit a cost impact proposal, and the basis used to develop the estimate. In most cases the estimate is developed from readily available data. If the auditor cannot provide the estimate, the report should give the reasons and identify the data needed to comply with the contracting official's request.

b. Cost Impact Proposal Submitted by Contractor - Where a cost impact proposal is submitted, either as a result of a finding of noncompliance by the auditor or as a voluntary action following changes made to established practices, it should initially be reviewed for adequacy of content and method of presentation.

If the proposed cost impact increases the Government's costs, the amount of the adjustment is the increase in cost to the Government over what the cost would have been if the contractor complied with the standards and followed consistently its disclosed or established practices.

Increased costs to the Government under firm fixed price contracts materialize when the costs allocated to the contracts are less than would have been allocated if the method of allocation had not been changed. For noncompliance on firm fixed price contracts, the amount of increased costs to the Government is the difference between cost estimates used in negotiations and the lower cost estimates that would have been used if the contractor had complied with the applicable CASB rules, regulations, and standards. For noncompliance on flexibly priced contracts, the increased cost to the Government is the difference between the current estimated cost at completion under the noncompliant method and the same estimate reconstructed under the compliant method.

Cost adjustments for either mandatory or voluntary changes should generally be the net difference between the current estimated cost to complete under the old accounting method and the same estimate reconstructed to reflect the new method.

The proposed cost effects and the related audit recommendations must be shown on a contract-by-contract basis to enable the contracting official to identify the affected contracts and determine the amount of the adjustment for each contract involved.

When a mix of contract types is involved, grouping contracts by type, by materiality of cost impact, or by other characteristics often simplifies the review process and also reduces the number of necessary price adjustments.

LISTING OF
COST ACCOUNTING STANDARDS
ISSUED BY THE
COST ACCOUNTING STANDARDS BOARD (CASB)

A complete list of the standards issued by the CASB and their effective and applicability dates are set forth below.

401. Consistency in Estimating, Accumulating and Reporting Costs -- effective and applicable July 1, 1972.
402. Consistency in Allocating Costs Incurred for the Same Purpose -- effective and applicable July 1, 1972.
403. Allocation of Home Office Expenses to Segment -- effective July 1, 1973, required to be followed as of the beginning of the next fiscal year after September 30, 1973.
404. Capitalization of Tangible Assets -- effective July 1, 1973, applicable to accrued expenditures for acquisition of tangible capital assets during the contractor's next fiscal year beginning on or after October 1, 1973.
405. Accounting for Unallowable Costs -- effective and applicable to all solicitations issued on or after April 1, 1974.
406. Cost Accounting Period -- effective July 1, 1974, required to be followed by each contractor as of the start of its next fiscal year beginning after receipt of a contract to which this standard applies.
407. Use of Standard Costs for Direct Material and Direct Labor -- effective October 1, 1974, required to be followed by each contractor as of the start of its next fiscal year beginning after the receipt of a contract to which this standard applies.
408. Accounting for Costs of Compensated Personal Absence -- effective July 1, 1975, required to be followed by each contractor as of the start of its next fiscal year beginning after the receipt of a contract to which this standard applies.
409. Depreciation of Tangible Capital Assets -- effective July 1, 1975, required to be followed by each contractor for all tangible assets acquired on or after the start of its next fiscal year beginning after the receipt of a contract to which this standard applies.
410. Allocation of Business Unit General and Administrative Expense to Final Cost Objectives -- effective October 1, 1976, required to be followed by each contractor after the start of its next fiscal year beginning after January 1, 1977.
411. Accounting for Acquisition Costs of Material -- effective January 1,

- 1976, required to be followed by each contractor on or after the start of its next cost accounting period beginning after the receipt of a contract to which this standard applies.
413. Adjustment and Allocation of Pension Cost -- effective March 10, 1978, required to be followed by each contractor on or after the start of its next cost accounting period beginning after the receipt of a contract to which this standard applies.
414. Cost of Money as an Element of the Cost of Facilities Capital -- effective October 1, 1976, but not applicable to contracts awarded or on which final agreement on price was reached prior to the effective date.
415. Accounting for the Cost of Deferred Compensation -- effective July 10, 1977, required to be followed by each contractor for awards of deferred compensation made on or after the start of its next cost accounting period beginning after the receipt of a contract to which this standard applies.
416. Accounting for Insurance Costs -- effective July 10, 1979, required to be followed by each contractor on or after the start of its next cost accounting period beginning after the receipt of a contract to which this standard applies.
417. Cost of Money as an Element of the Cost of Capital Assets Under Construction -- effective December 15, 1980, required to be followed by each contractor on or after the start of its next cost accounting period beginning after the receipt of a contract to which this standard applies.
418. Allocation of Direct and Indirect Costs -- effective September 20, 1980, required to be followed by each contractor on or after the start of its second fiscal year beginning after the receipt of a contract to which this standard applies.
419. (withdrawn and not replaced)
420. Accounting for Independent Research and Development Costs and Bid and Proposal Costs -- effective March 15, 1980, required to be followed by each contractor as of the start of its second fiscal year beginning after the receipt of a contract to which this standard applies.

**GUIDE FOR EXAMINING INTERRELATIONSHIPS OF
INFORMATION ON A CONTRACTOR'S
DISCLOSURE STATEMENT**

The following listing of interrelationships between various sections of a disclosure statement is designed to facilitate reviewing of the statement for accuracy:

1. If item 1.8.0 is marked A or B, item 2.2.1 or 2.2.2 should be marked A or item 2.5.0 should be coded C in at least one column.
2. A response in section 2.4.0 is required only if block A of items 2.2.1 or 2.2.2 is marked.
3. Section 2.6.0 should be completed only if one or more labor categories in item 2.5.0 were marked C.
4. If item 2.2.2 is marked A, B, C, D, or Y, item 3.2.1 (f) must be marked with a code other than Z.
5. If 4.1.0(a) is marked with a code other than Z, no other items in 4.1.0 are to be marked.
6. If items 4.2.0(a), (b), (c), or (d) are marked with a code other than Z, items (e) through (n) are not to be marked.
7. Item 3.2.3(s) must be marked other than F or Z if item 4.7.0(a) is to be marked A, B, C, or D. Item 3.2.3(k) must be marked other than F or Z if item 4.7.0(b) is to be marked A, B, C, D. Item 2.8.0 must be marked A, B, C, D or Y in at least one column if item 4.7.0(d) is marked A, B, C, or D.
8. If item 4.2.0(i) is marked with a code other than Z item 4.8.1 should be marked B or D.
9. If item 2.5.0 is checked for A, B, C, and/or Y in any column, at least column 1 of items 6.1.1 and 6.1.2 must be completed.
10. Item 7.1.1 cannot be blank. If item 3.2.2(d) is marked other than Z, item 7.1.1 must be marked A.
11. Item 7.1.2 cannot be blank or marked Z in all columns if item 7.1.1 is checked A. Under ERISA, item 7.1.2 may not be checked B.
12. Items 7.1.3, 7.1.4, 7.1.7, 7.1.8, and 7.1.9 cannot be blank in any column for which item 7.1.2 has been marked other than Z in the same column.
13. If item 7.1.2, line C, is marked in any column, item 7.1.6 must be marked on line A, B, C or Y in the same column.
14. If item 7.1.3 is marked B in any column, item 7.1.2 must be marked A, and item 7.1.6 must be checked Z in the same column.

15. If item 7.1.7 is marked other than Z in any column, item 7.1.8 must be marked on line A or B in the same column.
16. If item 3.2.2(a) is marked with a code other than Z, item 7.3.1 must be marked A, B, or C.
17. If item 7.3.1 is marked A or C, items 7.3.2, 7.3.3, 7.3.4, and 7.3.5 cannot be blank.
18. If item 7.3.1 is marked B or C, item 7.4.0 cannot be blank or marked Z.
19. At least one of items 8.3.1, 8.3.2 and 8.3.3 should have an entry against it if this part is being completed by a corporate, group, or home office.

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5 of 7

EXAMPLE OF COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT AUDIT REPORT

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITS

REVISED
COST ACCOUNTING STANDARDS BOARD
DISCLOSURE STATEMENT
ABC, INC.
CITY, STATE

REPORT NUMBER:

PURPOSE AND SCOPE

We audited ABC, Inc.'s (ABC) January 1, 1989, revised Cost Accounting Standards Board disclosure statement to determine if it adequately described the cost accounting practices that ABC proposes to use in performing Government contracts and subcontracts. The disclosure statement and related data are the responsibility of ABC. Our responsibility is to reach a conclusion on the adequacy of the disclosure statement.

The audit scope was limited to reviewing ABC's January 1, 1989, revised disclosure statement. We tested the accuracy of the revisions by comparing the disclosed practices with ABC's written accounting procedures and actual accounting practices. We did not evaluate the adequacy of the complete disclosure statement or determine if the disclosed practices complied with Cost Accounting Standards (CAS).

As defined in the above scope paragraph(s) we conducted our audit in accordance with generally accepted Government auditing standards that applied to this financial related audit. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the data and records reviewed are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records reviewed. An audit also includes assessing the accounting principles used and significant estimates made by the contractor, as well as evaluating the overall presentation. We used the provisions of Federal Acquisition Regulation Part 30 and CAS Part 351 as criteria in evaluating the adequacy of ABC's disclosure statement. We believe that our audit provides a reasonable basis for our audit conclusions.

We completed our onsite review on September 30, 1989.

AUDIT RESULTS

We conclude that ABC's revised disclosure statement adequately describes its cost accounting practices. This review was limited to ascertaining the

adequacy of the subject disclosure statement. Accordingly, we express no conclusion as to whether the disclosed practices are proper, %PAGES approved, or agreed for pricing proposals, accumulating costs, or reporting contract performance data.

JOHN DOE & COMPANY

By: _____

ACCEPTED BY:

INSPECTOR GENERAL

OFFICE OF

EXAMPLE OF ACCOUNTING SYSTEM AUDIT REPORT

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITSACCOUNTING SYSTEM AUDIT OF
ABC, INC.
CITY, STATE

REPORT NUMBER:

PURPOSE AND SCOPE

In response to a request from the U.S. Department of Energy (DOE), Field Office, Idaho, we audited ABC, Inc.'s accounting system. ABC is performing subcontract work for XYZ Corporation on a time-and-materials basis under DOE Contract No. DE-AC00-90AB00003. XYZ Corporation is considering changing this subcontract to a cost reimbursement subcontract.

The purpose of our audit was to determine the adequacy of ABC's accounting system for segregating, accumulating, and reporting costs under a cost-reimbursement subcontract.

The scope of the audit was limited to establishing the reliability of the accounting system to accurately identify and segregate costs by final cost objective. Accordingly, we audited policies, procedures, the chart of accounts, supporting documentation (such as job cost reports, payroll records, invoices, journal entries, and travel reports); and interviewed personnel. We also audited and evaluated internal controls to the extent considered necessary in the circumstances. We did not evaluate ABC's total internal control system.

As defined in the above scope paragraph(s) we conducted our audit in accordance with generally accepted Government auditing standards that applied to this financial related audit. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the data and records reviewed are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records reviewed. An audit also includes assessing the accounting principles used and significant estimates made by the contractor, as well as evaluating the overall presentation. Criteria used included the Federal Acquisition Regulations (FAR), DOE Acquisition Regulations (DEAR), and the Cost Accounting Standards (CAS). We believe that our audit provides a reasonable basis for our audit conclusions.

We completed our onsite work on January 25, 1990.

BACKGROUND

During a preaward audit of a time-and-material change order proposal to the subcontract with XYZ Corporation, we noted the following deficiencies with ABC's accounting system:

1. The time reporting system did not require salaried employees to record all hours worked.
2. ABC did not have formal written accounting procedures and policies for employee travel, purchasing, and fixed asset depreciation.
3. Vendor invoices for direct and indirect costs were filed inconsistently. Invoices for direct costs were filed in chronological order by the billing date. All other invoices were filed by vendor name.
4. Travel vouchers were prepared by ABC's office manager rather than the traveler. The travel vouchers did not document the approval of the traveler or an authorized supervisor.
5. ABC prepared invoices from source documentation rather than from the job cost ledger. Invoices were not reconciled to the job cost ledger. We noted posting errors that resulted in billed direct costs being posted to indirect expense accounts. As a result, double counting of expenses occurred because ABC did not prepare invoices from the accounting books and records, reconcile the invoices to the books and records, or verify the accuracy of the books and records used to prepare the Fiscal Year (FY) 1989 indirect cost rate proposal.

After discussions with a DOE Field Office, Idaho representative, we were requested to determine the adequacy of ABC's accounting system for segregating, accumulating, and reporting costs under a cost-reimbursement subcontract.

AUDIT RESULTS

The significant internal controls that ABC should maintain with respect to effectively administering cost-reimbursement subcontracts include controls designed to ensure that:

- o The breakdown of costs within the accounting system is adequate for cost determination purposes;
- o Specific cost elements are afforded consistent treatment regarding Government and non-Government cost objectives;
- o Allowable and unallowable costs are routinely identified and segregated in the accounting system;
- o Adequate source documentation supports all costs;
- o Assets are safeguarded against loss or unauthorized use or disposition; and

- o All accounting data are accurate, reliable, and traceable to underlying source documentation.

Our study and evaluation made for the limited purpose described in the preceding section would not necessarily disclose all material weaknesses in the system. Accordingly, we do not express a conclusion on ABC's internal accounting control system taken as a whole. Based on our evaluation of the significant internal accounting controls indicated above, we consider ABC's accounting system inadequate for the reasons described below.

We started the accounting system audit on January 10, 1990. ABC had hired a new accountant and was in the process of implementing a new accounting system. No accounting system documentation was available for FY 1990, which began on October 1, 1989, because transactions had not been posted to the ledgers and journal since September 30, 1989. Therefore, we were unable to assess the adequacy of ABC's new accounting system for segregating, accumulating, and reporting costs under a cost-reimbursement subcontract.

Our audit results regarding the deficiencies noted during the preaward audit follow:

1. The time reporting system still does not require salaried employees to record all hours worked.
2. ABC still does not have formal written accounting procedures or policies for employee travel, purchasing, and fixed asset depreciation for the prior accounting system or the system being implemented.
3. Vendor invoices for direct and indirect costs are still filed inconsistently. Invoices for direct costs are filed in chronological order by the billing date. All other invoices are filed by vendor name.
4. ABC has revised its travel policy and implemented a standard travel voucher that documents the review and approval by the traveler and an authorized supervisor.
5. ABC still prepares invoices from source documentation rather than from the job cost ledger, and invoices are not reconciled to the job cost ledger.

Additional deficiencies noted during the audit follow:

1. The proposed chart of accounts for the new accounting system does not segregate and accumulate bid and proposal costs.
2. The proposed chart of accounts for the new accounting system does not identify and segregate all unallowable costs.
3. The proposed chart of accounts for the new accounting system identifies overtime premium costs directly to the XYZ Corporation subcontract. Overtime premium should be an indirect expense allocable to all final cost objectives in proportion to the benefits received.
4. ABC does not currently have procedures for computing and billing the

effective hourly rate for salaried employees who work more than 40 hours per week without overtime compensation.

RECOMMENDATIONS

We recommend that DOE direct XYZ Corporation to require ABC to:

1. Ensure that all employees report all time worked.
2. Establish written accounting procedures and policies for employee travel, purchasing, and fixed asset depreciation.
3. File all vendor invoices in a consistent manner.
4. Ensure that the standard travel voucher is used consistently and is approved by the traveler and an authorized supervisor.
5. Prepare invoices from the job cost ledger and ensure the accuracy of postings to the ledger.
6. Establish an adequate chart of accounts that segregates bid and proposal costs and unallowable costs. In addition, ensure that the chart of accounts identifies and allocates overtime premium costs to final cost objectives in proportion to the benefits received.
7. Establish procedures for computing effective hourly rates for salaried

AUDIT GUIDE
COST ACCOUNTING STANDARDS COMPLIANCE REVIEWS

This exhibit provides guidance in auditing the implementation of specific CAS. The guide is to be used in conjunction with the actual CAS (CASB) promulgations, applicable contract cost principles and procedures, and other pertinent provisions.

CASB promulgations illustrate the application of each standard. Additional examples are cited below to amplify the CASB guidance. Most examples are extracted from the DCAA Contract Audit Manual.

Most DOE contracts are not subject to CAS. However, since these standards generally represent the codification of accounting practices that Government contractors have followed for many years, they can be considered generally accepted accounting practices.

In addition, many of the standards have been incorporated into the FAR cost principles. The auditor should keep in mind that the CAS should be cited as the basis for questioning a contractor's practices/costs only when the related contract is CAS covered. If the contract is not subject to CAS, the applicable FAR cost principles or other applicable bases should be cited.

CAS 401 - CONSISTENCY IN ESTIMATING, ACCUMULATING AND REPORTING COST. The purposes of this standard are (1) to achieve consistency in the cost accounting practices used by a contractor in estimating costs for its proposal with those practices used in accumulating and reporting costs during contract performance and (2) to provide a basis for comparing such costs.

Noncompliance with the standard can exist because a contractor has failed to estimate its cost in accordance with its established or disclosed accounting practices; noncompliance can also occur when a contractor estimates in accordance with its disclosed or established practices but accumulates on a different basis without obtaining prior approval from the Government.

1. Consistency Between Estimating and Accumulating Costs. The grouping of homogeneous costs for proposal purposes does not result in noncompliance when the costs are accumulated and reported in greater detail on an actual cost basis during contract performance. The following are two selected examples of permissible groupings of costs as presented in the Standard (section 401.60(a)):

- o Contractor estimates an average direct labor rate for manufacturing direct labor by labor category or function. Contractor records manufacturing direct labor based on actual cost for each individual and collects such costs by labor category or function.
- o Contractor uses an estimated rate for manufacturing overhead to be applied to an estimated direct labor base. Contractor identifies the items included in its estimate of manufacturing overhead and provides supporting data for the estimated direct labor base. Contractor accounts for manufacturing overhead by individual items of cost which are accumulated in a cost pool allocated to final cost objectives on a direct labor base.

Noncompliance can occur when the estimate is prepared in greater detail than the practices followed to accumulate and report costs, as indicated by the following example in the Standard (section 401.60)):

Contractor estimates engineering labor by cost function, i.e., drafting, production, engineering, etc. Contractor accumulates total engineering labor in one undifferentiated account.

If the contractor's estimates are in accordance with this baseline and are in greater detail than costs in the records, the auditor should normally recommend that costs be accumulated in a manner consistent with the estimate.

CASB Interpretation No. 1 to CAS 401 provides that contractors who estimate material losses by applying a percentage factor to a base such as total material requirements must support the factor with experience. The contractor should be cited for noncompliance only when the unsupported scrap factors are applied to totals or subtotals of material requirements. Where the contractor adjusts the quantities of individual line items in the bill of material, either by applying a factor or by adding a specific quantity of additional units, the contractor complies with the standard.

2. Consistency in Reporting Costs - The following examples may serve as a guide in determining compliance with the standard.

- o A contractor proposes the cost of engineering labor by class, i.e., Engineer I, Engineer II, etc. However the contractor's practice is to accumulate engineering labor by type, i.e., Electrical Engineer, Design Engineer, etc. Such practice would violate CAS 401. If the contractor were to submit a summary of the labor costs by type of engineer, which reconciled with the proposed cost by class of engineer, and further explained that cost would be accumulated in this manner, then the practice would comply with CAS 401.
- o A contractor estimates cost by line item but does not intend to accumulate the cost of each item separately. Rather, in accordance with its established accounting practice, the contractor accumulates labor, material, and indirect costs for the contract as a whole. This practice does not comply with CAS 401. Where the contractor elects to estimate and accumulate the combined costs of several line items by cost elements (direct labor, material, indirect costs, etc.), such a practice does not necessarily violate CAS 401. But if the Government requires estimates by individual line item, the contractor must accumulate costs in the same manner.
- o A contractor prepares separate estimates for the cost of raw materials, subcontracts, purchased parts and interdivisional transfers. The costs of these items are not separately identified in the accounting records. The practice is in noncompliance with the standard and the contractor should be required to accumulate costs consistent with its estimates. However, the standard permits supplemental records to be maintained if they can be reconciled to the formal accounting records.

- o A contractor uses a material additive factor to cover the cost of small, common-usage items. In preparing the price proposal, the cost of this factor is estimated as an historical percentage of direct material requirements. In accumulating costs, these items are computed as a percentage of direct productive labor hours. The condition described above contravenes the provisions of CAS 401. The auditor should report the noncompliance and recommend that the contractor change its actual practices to conform with its disclosed or established practices.

CAS 402 - CONSISTENCY IN COSTS INCURRED FOR THE SAME PURPOSE. The purpose of this standard is to ensure that each type of cost is allocated only once and on only one basis to any contract or other cost objective. The fundamental requirement is that all costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives. Following is a discussion of four situations which further explain the CAS requirement.

1. Proposal Costs. Costs of preparing proposals will be treated as indirect costs except where contract provisions specifically require such effort. Proposal costs incurred pursuant to the specific requirement of an existing contract are considered to have been incurred under different circumstances than other proposal costs and may be charged direct to the contract.
2. IR&D Costs. A contractor charges engineering consultant costs incurred on IR&D projects to engineering overhead. The same costs incurred for research and development contracts are charged direct to the contract. The practice does not comply with the standard because the same type of costs, incurred in similar circumstances, are charged to cost objectives on different bases. Where benefiting projects can be specifically identified, the consultant costs should be charged directly to those projects.
3. Personnel Dedicated to a Contract. A contractor has a Government contract which requires extra effort for planning and cost management. It hires additional employees to accomplish this effort and accounts for all its labor cost as a direct charge to the contract. The contractor has other employees performing the same functions for more than one contract and their labor is charged to indirect costs.

Since the work being performed is the same and the only difference is the amount of effort required to accomplish the function, this practice does not comply with the standard. The contractor could correct the situation by (1) charging all these costs to indirect expenses and developing an equitable distribution base or (2) direct charging all the costs.

4. General Purpose vs. Special Purpose Facilities and Equipment. A contractor has hundreds of cranes located throughout a shipyard. Maintenance, taxes, and depreciation costs are recorded in a general account and then allocated to departmental overhead pools for distribution to contracts. The dry dock has the cost of eight cranes charged directly to its departmental overhead pool, because their use is unique to the dry dock operations. Since the dry dock cranes are used for a special purpose and the yard cranes for general purposes, this practice would not result in double counting. However,

if any yard cranes are also used for a special purpose, the practice would result in double counting and would not comply with the standard. Under those conditions all the special purpose cranes should be eliminated from the general account and charged directly to the using department to correct the problem.

CAS 403 - ALLOCATION OF HOME OFFICE EXPENSES TO SEGMENTS. The purpose of this standard is to establish criteria for allocating the expenses of a home office to the segments of the organization on the basis of a beneficial or causal relationship. The appropriate implementation of this standard limits the amount of home office expenses classified as residual to the expenses of managing the organization as a whole.

The standard recognizes that some home office expenses incurred for specific segments can be assigned directly. Other expenses, not incurred for specific segments, have a clear relationship (i.e., measurable with reasonable objectivity) to two or more segments. The standard also recognizes a third type of home office expense (i.e., residual) which possesses no readily measurable relationship to segments. Consistent with this concept of home office expenses, the standard requires that:

- o Those expenses incurred for specific segments are to be allocated directly to those segments to the maximum extent practical.
- o Those expenses not directly allocable but possessing an objective, measurable relationship to segments should be grouped in logical and homogeneous expense pools and distributed on allocation bases reflecting the relationship of the expenses to the segments concerned.
- o When the residual expenses are considered material because they exceed a specific percentage of total company operating revenue (as defined in section 403.40[c][2]), a three-factor formula must be used to allocate these expenses. If the residual expenses do not exceed this threshold, they may be allocated to all segments by means of any allocation base representing the total activity of such segments.

Basically, to ascertain whether the accounting practices comply with the standard, the auditor should determine if (1) the expenses have been properly classified as directly allocable, indirectly allocable, or residual, (2) the "logical and relatively homogeneous pools" are allocated on bases reflecting the relationship of the expenses to the segments concerned, and (3) the residual expenses are allocated on a base "representative of the total activity" of the company or the prescribed three-factor formula.

A careful reading of the entire standard is necessary to cover any special situations.

CAS 404 - CAPITALIZATION OF TANGIBLE ASSETS. This standard establishes criteria for determining the acquisition cost of tangible assets which are to be capitalized. It does not cover depreciation or disposition of fixed

assets, which CAS 409 covers. The standard requires contractors to have a written policy which designates economic and physical characteristics for capitalization, including the following:

- o A minimum service life of 2 years and a minimum acquisition cost criterion of \$1,000. However, both these criteria may be reduced, if desired.
- o The identification of asset accountability units to the maximum extent practical.
- o The establishment of minimum dollar amounts for the capitalization of original complements of low cost equipment.
- o The capitalization of tangible capital assets constructed or fabricated by a contractor for its own use at amounts which include costs properly allocable to such assets, i.e., factory overhead, G&A expenses (when material in amount) and, in addition, cost of money (CAS 414 and 417).

The standard also provides for the capitalization of donated assets at the fair value of the asset acquired and furnishes criteria for the assignment of a portion of the cost of an acquired company to its tangible assets. In this regard, the criteria agrees with the requirements of Accounting Principles Board Opinion number 16, Business Combinations.

Note that this standard does not apply to facilities and equipment acquired or constructed for the Government; it applies only to assets constructed or acquired for the contractor's own use.

Following is an example of an incorrect and a correct indirect expense allocation to a capital asset constructed for the contractor's own use.

The contractor manufactures Model X for the Government. The contractor produces one unit of Model X for its own use. The contractor capitalized the asset at \$37,500 (\$25,000 material, \$5,000 production labor, and \$7,500 overhead, reflecting a 150 percent annual overhead rate). When constructed assets are identical with the contractor's regular product, such assets must be allocated their full share of indirect costs, including G&A expenses and cost of money (CAS 404.50(b)). Assuming that G&A expenses, production overhead cost of money, and G&A expense cost of money rate for the year are 10 percent, 10 percent, and 1 percent respectively, the asset should have been capitalized at \$42,180, computed as follows:

Material		\$25,000
Production Labor		5,000
Production Overhead	(150%)	7,500
Cost of Money related to Production		
Overhead	(10%)	<u>500</u>
Subtotal		38,000
G&A Expense	(10%)	3,800
Cost of Money related to G&A		
Expense	(1%)	<u>380</u>
		<u>\$42,180</u>

CAS 405 - ACCOUNTING FOR UNALLOWABLE COSTS. The purpose of this standard is to facilitate the negotiation, audit, administration, and settlement of contracts. It contains guidelines on (1) identification of costs specifically described as unallowable, at the time such costs first become defined or authoritatively designated as unallowable and (2) the cost accounting treatment to be accorded such identified unallowable costs in order to promote the consistent application of sound cost accounting principles covering all incurred costs. The standard does not govern the allowability of costs which is a function of contracting officials.

The fundamental requirements of this standard are expressly stated in FAR 31.201-6. In short, costs that are expressly unallowable or mutually agreed to be unallowable, including mutually agreed to be unallowable directly associated costs, must be identified and excluded from any billing, claim, or proposal applicable to a Government contract. FAR paragraphs 31.201-6(d) and (e) provide guidance for determining when directly associated costs are sufficiently material to warrant disallowance.

The purpose of this standard is to provide criteria for selecting the time periods to be used as cost accounting periods for contract cost estimating, accumulating, and reporting. It reduces the effects of variations in the flow of costs within each cost accounting period. It also enhances objectivity, consistency, and verifiability and promotes uniformity and comparability in contract cost measurements. The illustrations which are part of the standard convey guidance for auditing compliance with this standard.

CAS 406 - COST ACCOUNTING PERIOD. The purpose of this standard is to provide criteria for selecting the time periods to be used as cost accounting periods for contract cost estimating, accumulating and reporting. It reduces the effects of variations in the flow of costs within each cost accounting period. It also enhances objectivity, consistency, and verifiability and promotes uniformity and comparability in contract cost measurements. The illustrations which are part of the standard convey guidance for auditing compliance with this standard.

CAS 407 - USE OF STANDARD COSTS FOR DIRECT MATERIAL AND DIRECT LABOR. The purpose of this standard is to provide criteria under which standard costs may be used for estimating, accumulating, and reporting costs of direct material

and direct labor. The standard also provides criteria relating to the establishment of standards, accumulation of standard costs, and accumulation and disposition of variances from standard costs. The illustrations which are part of the standard convey suitable guidance for auditing compliance with it.

CAS 408 - ACCOUNTING FOR COSTS OF COMPENSATED PERSONAL ABSENCE. The purpose of this standard is to establish criteria for measuring and allocating the costs of compensated personal absences to final cost objectives. These costs include compensation paid by contractors to their employees for such benefits as vacations, sick leave, holiday, military leave, etc. The provisions of the standard require that the costs of compensated personal absence be assigned to the cost accounting period in which entitlement is earned in accordance with the contractor's plan or custom. The illustrations which are part of the standard convey guidance for auditing compliance with the standard.

CAS 409 - DEPRECIATION OF TANGIBLE CAPITAL ASSETS. This standard provides criteria and guidance for assigning costs of tangible capital assets to cost accounting periods and for allocating the costs to cost objectives in a consistent manner. A careful reading of the standard and FAR 31.205-11 is necessary before determining whether a contractor's depreciation practices comply with the standard. The following illustrative applications augment those included in the standard.

- o Depreciation expense was allocated to manufacturing overhead. Gains and losses on sale should also be allocated to manufacturing overhead. Following is the financial history of three machines, each 7 years old, which were recently sold and the allocation to overhead:

<u>Capital Equipment</u>	<u>Capitalized Acquisition Cost</u>	<u>Current Net Book Value</u>	<u>Sales Price</u>	<u>Allocation to Overhead Gain/(Loss)</u>
Lathe	\$30,000	\$10,000	\$32,000	\$20,000*
Truck	5,000	-0-	100	100
Fork Lift	10,000	3,000	2,000	(1,000)

* Gain or loss is the difference between amount realized on disposition and its undepreciated balance (\$32,000 - \$10,000 = \$22,000); however, per CAS 409.50(j)(1), for contract costing purposes, the gain must be limited to the difference between the original acquisition cost of the asset and its undepreciated balance (\$30,000 - \$10,000 = \$20,000).

- o In another illustration the capitalized cost of a lathe is \$50,000. The lathe is projected to have residual value of \$4,500 and an estimated service life of 10 years. The contractor utilizes a straight line depreciation method. Because the \$4,500 residual value is less than 10 percent of the capitalized cost, the annual depreciation charges may be based on a depreciable cost base of \$50,000. However, since section 409.50(h) provides that no

depreciation costs will be charged which would significantly reduce an asset below its residual value, the depreciation cost in the 10th year should be reduced to \$500, as computed below:

Depreciable cost base		\$50,000
Accumulated depreciation		
9 years @ \$5,000 per year	\$45,000	
10th year @ 500	500	
		<u>45,500</u>
Net book value at end of 10th year (equals residual value)		<u>\$ 4,500</u>

CAS 410 - ALLOCATION OF BUSINESS UNIT GENERAL AND ADMINISTRATIVE EXPENSES TO FINAL COST OBJECTIVES. This cost accounting standard provides criteria for the allocation of general and administrative (G&A) expenses to final cost objectives and furnishes guidelines for the type of expense that should be included in the G&A expense pool. It also requires that G&A expense be allocated on a cost input base representing total activity. The cost input base selected may be total cost input, value-added cost input, or single-element cost input. A value added cost input base is total cost input less material and subcontract costs. Direct labor dollars are an example of a single element cost input base. Contractors presently using the sales or cost of sales allocation base have the option of (1) changing to the cost input allocation base as soon as they become subject to the standard or (2) selecting the special transition method described in Appendix A of the standard.

The illustrations in the standard are fairly extensive and should provide adequate guidance when carefully considered in the context of the application techniques in the standards.

CAS 411 - ACCOUNTING FOR ACQUISITION COSTS OF MATERIALS. This standard provides criteria for the accounting of acquisition costs of material and also furnishes guidance on using inventory costing methods. The standard does not cover accounting for the acquisition costs of tangible capital assets nor accountability for Government-furnished materials.

CAS 412 - COMPOSITION AND MEASUREMENT OF PENSION COSTS. This standard establishes the composition of pension costs, the basis of measurement, and the criteria for assigning pension costs to cost accounting periods. CAS 413 addresses the accounting treatment of actuarial gains and losses and the allocation of pension costs to segments of an organization.

The standard is basically compatible with the Employee Retirement Income Security Act of 1974 (ERISA), although some of its provisions may be more restrictive than ERISA funding requirements. The fundamental objectives of CAS 412 differ from the objectives of ERISA. ERISA is primarily a funding law; it is designed to ensure financial integrity of pension plans through minimum funding standards. CAS 412 was promulgated to ensure that pension costs are properly measured and allocated to cost objectives.

Under a defined contribution plan, the pension cost of a cost accounting period is the net contribution required to be made, after adjustment for dividends and other credits. For a defined benefit plan the pension cost for a period may consist of four elements as follows.

- o Normal cost (annual cost attributable to years after a particular valuation date).
- o Amortization of the unfunded actuarial liability (excess of the actuarial liability over the value of the pension fund assets).
- o Interest equivalent on the unfunded actuarial liability and actuarial gains or losses being amortized.
- o Adjustment for actuarial gains and losses (differences between forecasted assumptions and actual experience).

By recognizing the interest equivalent, as mentioned above, CAS 412 allows interest despite the prohibitions in the cost principles, but 412.50(a)(7) does not permit the recognition of interest occasioned by contractor's failure to fund a periodic payment to the plan.

The standard does not require the use of a specific actuarial cost method; however, the method selected by the contractor must provide for separate measurement of the pension cost elements listed above. The cost elements are identified under the accrued benefit method and some of the projected benefit cost methods. They are not identified under certain methods, which neither disclose actuarial gains and losses nor develop the amount of unfunded liability. If the projected benefit cost method used does not separately measure the cost elements, the method will be considered acceptable only if:

- o The method is used for financial accounting.
- o An alternative computation is made (under a projected benefit cost method -- i.e., entry age normal -- which separately identifies normal costs, unfunded actuarial liabilities, and actuarial gains and losses) to disclose the funding status of the plan and if pension cost assigned to the cost accounting period is reduced by any excess funding. The plan is excessively funded if the value of the pension fund assets exceed the actuarial liability.
- o Supplementary records are maintained to identify all actuarial gains and losses and show their disposition.
- o The cost of future benefits is spread over the remaining average working lives of the work force.

Pension costs applicable to prior periods which were specifically unallowable under then-existing contractual provisions should be separately identified and excluded from an amortization of unfunded liability or from future normal costs if the actuarial cost method in use does not separately

develop an unfunded actuarial liability. Excise taxes and interest costs incurred as a result of inadequate or delayed funding are not considered components of pension costs.

1. Funding Method. The compliance review should identify the actuarial method used by the contractor for each plan in effect. Review actuarial reports and statements and related accounting records. If projected benefit methods do not separately identify the pension cost elements, review the contractor's proposed procedure for developing the required supplementary information and the computations made thereunder. If the contractor has previously completed a disclosure statement, determine if the block checked for item 7.1.3 -- Actuarial Cost Methods complies with the standard's provisions. Blocks "B" through "G" of item 7.1.3 represent variants of projected cost methods which will trigger the visibility requirements in paragraph 412.50(b) of the standard. If response "B -- Aggregate," "C -- Attained age -- Initial Liability Frozen," "E -- Entry Age -- Initial Liability Frozen," and "G -- Individual Level Premium" are checked, the alternative computation and supplementary information requirements of paragraph 412.50(b)(2) will be applicable.

2. Amortization Period for Unfunded Liabilities. Item 7.1.6 should be reviewed to determine whether any changes in amortization periods which are required by the standard are properly reflected in the disclosure statement. Part 412.50(a)(3) of the standard requires a contractor to establish and consistently follow a policy for selecting specific amortization periods for unfunded actuarial liabilities. An acceptable pension amortization plan does not necessarily have to result in a straight line writeoff of past service pension costs. Under the contractor's procedure, the number of years to be considered in determining the annual amortized amount may vary from year to year. As an example, a contractor may maintain a variable amortization schedule in which (1) the amortization period is based on the ratio of pension assets to pension liabilities and (2) the determination of the amortization period is made annually based on the ratio of pension assets to pension liabilities in that year. In this situation, the change in amortization period is not considered a change in accounting practice, since it is in accordance with an established policy. The contractor should describe in writing the practice for setting the amortization period. Be alert to situations reflecting a deviation from established procedures governing the variable aspects of the plan. Ideally, forces that are largely external to the contractor's operations, such as market conditions, general business and employment levels, etc., should trigger those factors that determine the amortization period. It is important to ascertain whether the plan is applied consistently. Unauthorized deviation from the established plan should be cited as noncompliance.

3. Compliance Review. The compliance review should include steps to identify and evaluate the reasonableness of the assumptions and to monitor actuarial gains and losses to assure that the assumptions remain valid. Following are two additional illustrations for aiding in determining compliance with the standard.

- o A contractor uses the aggregate cost method for computing and funding the \$2.3 million pension costs assignable to the period. Since the aggregate method does not provide the cost visibility

required by the standard, the contractor, for the fiscal year just ended, made the alternative calculation using the entry age normal method and provided supplementary information on actuarial gains and losses. The contractor's analysis disclosed that at fiscal yearend (1) the value of the pension fund assets was \$12.6 million, (2) the actuarial liability was \$10 million, and (3) the experienced actuarial gain for the period was \$1 million. According to paragraph 412.50(b)(2) of the standard, the pension cost to be allocated to contracts for the cost accounting period is zero, since the amount of overfunding (\$2.6 million) exceeds the computed cost for the period (\$2.3 million). Furthermore, the significance of the experienced actuarial gain would indicate that the actuarial assumptions may not be reasonable. The contractor should be required, according to paragraph 412.50(b)(7) of the standard, to identify the actuarial assumptions which were responsible for the gain and to provide rationale for either retaining or revising those assumptions.

- o As a result of a temporary cash shortage, a contractor's payments into the pension fund did not meet the Employment Retirement Income Security Act (ERISA) of 1974 funding requirements for the period. A 5 percent excise tax on the accumulated funding deficiency was, therefore, assessed against the contractor. In computing the pension cost for the fiscal year, the contractor included the assessment of the 5 percent tax plus an interest equivalent on the unpaid amount. Both the excise tax, which was assessed as a penalty for the delayed payment, and the interest equivalent on the delayed payment should be excluded from pension costs allocated to Government contracts according to paragraphs 412.50(a)(6) and (7) of the standard. The CASB, in its prefatory comments to the standard, acknowledged that an interest equivalent should be recognized to determine whether a pension plan is properly funded. However, since interest resulting from delayed funding is caused by a management decision to use funds for other purposes, the interest should be considered as investment cost rather than as a component of pension cost.

CAS 413 - ADJUSTMENT AND ALLOCATION OF PENSION COST. This standard establishes criteria for (1) assigning actuarial gains and losses to cost accounting periods, (2) valuing pension fund assets, and (3) allocating pension costs to segments.

Provisions in the standard are somewhat more stringent than ERISA requirements concerning frequency of actuarial valuations and methods of valuing pension fund assets. Consequently, some accounting changes may be required to comply with the standard, in addition to those which were previously made to comply with ERISA.

Segment data for termination experience, age distribution, and actuarial assumptions for termination, retirement age, or salary scale will generally not be included in actuarial reports, CPA reports, Schedule B to IRS Form 5500, or other pension source documents. Thus, the auditor should try to

learn, at the onset of the pension review, the segment data that the contractor has to provide to permit an audit determination of compliance with CAS 413.50(c)(2) and (3). Two illustrations follow:

- o Contractor X was acquired by Contractor Y and renamed Segment B. Y retained X's entire work force following the acquisition. Pursuant to terms of X's pension plan, X employees were paid all vested pension benefits at the time of dissolution of X. The employees, upon coming to work for Contractor Y, were considered "new employees" with no actuarial liability attributable to their past service with Contractor X. Contractor Y's unfunded actuarial liability at the time of the merger was \$25 million. Contractor Y has consistently made a composite pension cost calculation for all of its segments and wishes to continue doing so.

Since Y's pension plan had a disproportionately larger unfunded actuarial liability than X's plan at the time of acquisition (i.e. \$25 million versus \$0), any combining of assets and actuarial liabilities of the two plans would result in a materially different pension cost allocation to Y's segments than if pension costs for Segment B were computed as though it had a separate pension plan. Pension costs must be calculated separately for Segment B.

- o Contractor X computes pension costs separately for Segments A, B, and C. As permitted in 413.50(c)(9), the contractor elects to establish a separate segment for inactive plan participants. Pension costs for the inactive segment are allocated back to A, B, and C on the ratios of the remaining working lives of the work force of the three segments. This method results in the following allocation of inactive segment pension costs:

	<u>Costs</u> <u>(in millions)</u>	<u>Percent</u>
Segment A	\$ 2.5	25
Segment B	4.0	40
Segment C	<u>3.5</u>	<u>35</u>
Total inactive segment cost allocated	<u>\$10.0</u>	<u>100</u>

The actuarial report discloses that the inactive plan participants retired from the following segments:

<u>Segment</u> <u>Retired from</u>	<u>Number of</u> <u>Retirees</u>	<u>Percent</u>
A	5950	85
B	350	5
C	<u>700</u>	<u>10</u>
	<u>7000</u>	<u>100</u>

Due to the geographical dispersion of the three segments, few employees had transferred among segments prior to retirement. The high ratio of retirees from Segment A was attributable to a major plant layoff which had occurred 10 years previously.

The contractor's allocation of inactive segment costs to Segments A, B, and C results in a substantially different amount than would have been allocated if a separate segment for inactive participants had never been established. The auditor should recommend an allocation of inactive segment costs to A, B, and C based on the ratio of the number of retirees from each segment to total retirees.

CAS 414 - COST OF MONEY AS AN ELEMENT OF THE COST OF FACILITIES CAPITAL. No guidance is provided at this time but will follow.

CAS 415 - ACCOUNTING FOR THE COST OF DEFERRED COMPENSATION. The purpose of this standard is to provide criteria for measuring deferred compensation costs and assigning such costs to cost accounting periods. It applies to all deferred compensation costs except for compensated absences and pension costs covered in CAS 408 and CAS 412. Suggested audit steps follow:

- o Determine whether the plan meets all the conditions necessary to constitute a financial obligation.
- o Determine whether the plan establishes a sound basis for prorating costs between accounting periods.
- o Ascertain whether the treasury rate is being applied correctly in present-value calculations of future benefits.
- o Review costs for proper credit of estimated forfeitures, based on past experience and future expectations, where deferred compensation costs are accounted for on a group basis.
- o For awards of assets other than cash, ascertain whether the plan provides for claimed market values of assets to be supported by a valid appraisal from an independent source.
- o Ascertain whether costs related to stock options, stock appreciation rights, and phantom stock plans are based on the dictates of FAR 31.205-6(i).

CAS 416 - ACCOUNTING FOR INSURANCE COST. This standard provides criteria for measuring insurance costs, assigning the costs to cost accounting periods, and allocating the costs to cost objectives. The fundamental requirement of the standard states that the amount of insurance costs to be assigned to a cost accounting period is the projected average loss for that period plus insurance administration expenses for the period. It also calls for the costs to be allocated to cost objectives based on causal or beneficial relationships.

A major difference between CAS 416 and FASB Statement 5, Accounting for Contingencies, is that FASB Statement 5 does not permit an accrual for loss contingencies unless certain conditions are met. A self-insurance charge

which only represents exposure to risk of loss cannot be accrued, as it can under CAS 416, under a self-insurance program. Therefore, a contractor may have to maintain memorandum records to reflect material differences between insurance costs stated in the financial records and the CAS 416 costs proposed on Government contracts.

1. Purchased Insurance. Under purchased insurance programs, the premiums or payments, adjusted by any refund, normally represent the projected average loss.

2. Self Insurance. Under self-insured programs the standard calls for the projected average loss to be "a self-insurance charge for each period for each type of self-insured risk" (416.50(a)(2)). Audits of selfinsurance costs will, therefore, require considerably more effort, since the reasonableness of the contractor's estimated accruals must be established. The audit of self-insurance charges under this standard should include a review of CAS 416, FAR Subpart 28.3, and the following:

- o A review of the contractor's overall self-insurance program and the adequacy of supporting records;
- o An analysis of the nature, amount, and pattern of actual insurance losses;
- o An evaluation of the contractor's method of estimating projected average loss from actual loss data; and
- o A comparison of the self-insurance charge with the cost of purchased insurance when it is available.

The following illustrations may aid in evaluating self-insurance.

- o A contractor establishes an approved self-insurance program to cover employee group health plans beginning with its next accounting period. The contractor makes a self-insurance charge based on analysis of employee claims submitted over the prior 10 years and an evaluation of anticipated conditions. The auditor determines that a well-known insurance company offers coverage at a cost materially lower than the selfinsurance charge. The contractor refuses to purchase insurance, because the insurance company is a subsidiary of a competitor and has a poor reputation. In this case the contractor's practice complies with CAS 416 even though purchased insurance is available at a lesser cost. Paragraph 5 of the supplemental information published with CAS 416 states that the limitation in CAS 416.50(a)(2)(i) is intended to apply only when the cost of comparable purchased insurance is used as a convenient method of estimating the projected average loss. The contractor's action is still subject to the test of reasonableness (FAR 31.2013). The difference between the cost of selfinsurance, plus administrative expenses, and purchased insurance should be disallowed if there is sufficient evidence that the contractor's reasons for using self-insurance are not valid.
- o A contractor proposes to discontinue its purchased insurance

coverage and become self-insured without setting aside specific financial resources to cover future losses. If the selfinsurance charge is measured and allocated properly following the criteria in CAS 416.50(a)(2), the proposed practice complies with the standard regardless of the availability of specific financial resources to cover future losses. The same cost, however, may be unallowable under the contract cost principles if the contracting officer has not approved the self-insurance program.

CAS 417 - COST OF MONEY AS AN ELEMENT OF THE COST OF CAPITAL ASSETS UNDER CONSTRUCTION. These standards recognize the allowability of the cost of money used for constructing or acquiring facilities. The standards provide criteria for measuring and allocating an appropriate share of the cost of the money which can be identified with the facilities employed in a business.

The FAR contract cost principles also recognize the allowability of the cost of money used for constructing or acquiring facilities, regardless of the applicability of CAS to a particular contract, provided it is measured and costed according to the CAS. From an audit standpoint, review of a contractor's computation of the cost of money will occur on individual price proposals, forward-pricing rate agreements, and in the establishment of final indirect cost rates.

In a compliance review, it is important to ascertain whether the contractor has established procedures and controls necessary to compute cost of money for the above activities. It is also necessary to determine (1) the correctness and validity of computed average net book values and (2) if the assets are being used in regular business activities.

CAS 418 - ALLOCATION OF DIRECT AND INDIRECT COSTS. CAS 418 requires the consistent classification of costs as direct or indirect, establishes criteria for accumulating indirect costs in indirect cost pools, and provides guidance on allocating these costs. The standard's fundamental requirements provide that (1) a business unit shall have a written statement of accounting policies and practices classifying costs as direct or indirect which shall be consistently applied; (2) indirect costs shall be accumulated in homogeneous indirect cost pools; and (3) pooled costs shall be allocated to cost objectives in reasonable proportion to the beneficial or causal relationships of the pooled costs to cost objectives.

1. Written Policies. The requirement for a written statement of accounting policies for classifying costs as direct or indirect is a critical aspect for assuring consistent implementation of this standard. If information disclosed by the contractor in "Part III, Direct vs. Indirect," Item 3.1.0, of the Disclosure Statement does not meet this requirement, the contractor should be requested to furnish additional detail.

2. New Pools. Additional indirect cost pools should be required only if the changes will result in materially different cost allocations. Materiality is emphasized in evaluating any perceived need for change in cost accounting practices. Materiality criteria are in the CASB Rules and Regulations, Part 331.71. When a noncompliance condition is not reported because the amounts are not material, periodic reviews are required to ascertain that the amounts remain immaterial.

Where the contractor is establishing new, indirect cost pools, careful attention should be directed toward whether the pools meet the requirements of the standard. Audit considerations, applicable to conditions both before and after a pool is established, should include propriety of the allocation base, homogeneity of the cost pools, and materiality.

Two illustrations are presented to aid in the review for compliance.

- o A contractor proposes to establish an allocation method for the central reproduction cost center. The contractor wants to use the number of personnel in each department as the basis for cost allocation. A central reproduction cost center does not contain a material amount of management and supervision of activities involving direct labor and direct material. Hence, the selection of a base is governed by CAS 418.50(e) which states that the best representation of the beneficial and causal relationship between this type of indirect cost pool and the benefiting cost objectives is a measure of resources consumption of the activities of the indirect cost pool. Number of personnel is a surrogate for resource consumption which may or may not represent the benefiting or causal relationship between the cost center and the benefiting cost objectives. Before accepting this base, the availability of more preferred measures, such as output of the activities of the indirect cost pool, should be determined.
- o An audit of a contractor reveals that several indirect cost pools contain costs of significant activities having dissimilar beneficial or causal relationships to cost objectives to which each pool is allocated. Further analysis indicates that allocation of the costs of the activities included in the cost pool result in an allocation to cost objectives which is not materially different from the allocation that would result if the costs of the activities were allocated separately. The contractor's practice complies with CAS 418.50(b)(1). However, if the amounts allocated are expected to be materially different in the future, the condition should be reported. In other cases, periodic followup reviews should be performed to ascertain whether changed circumstances have caused allocation differences to become material.

CAS 420 - ACCOUNTING FOR INDEPENDENT RESEARCH AND DEVELOPMENT COSTS AND BID PROPOSAL COSTS. This standard provides criteria for accumulating IR&D/B&P costs and for allocating such costs to cost objectives based on the beneficial or causal relationship between such costs and cost objectives.

The standard provides that IR&D/B&P costs are to be accumulated by project and that the project costs shall consist of all allocable costs except business unit G&A expenses. Under specific conditions, costs of IR&D/B&P projects performed by a segment but benefiting more than one segment must be accumulated at the home office. Home office IR&D/B&P costs are to be allocated to segments through (1) allocation to specific segment(s) when beneficial or causal identification can be made or (2) use of the CAS 403 residual expense allocation base. Special allocations are also permitted IR&D/B&P costs accumulated at segments (including home office allocations and

transfers from other segments) will be allocated to final cost objectives using the same base used for G&A expenses under CAS 410. However, special allocations are permitted when a particular final cost objective receives significantly more or less benefit from IR&D or B&P costs than would result from using this base.

The requirements for accumulating IR&D/B&P costs by project and home office accumulation of IR&D/B&P projects benefiting more than one segment increase the need for maintaining close coordination between the home office auditor and auditors at the operating segments. Project identification must be retained on costs transferred from a segment to a home office in order that appropriate allocations from the home office to all benefiting segments can be accomplished. The coordination process includes reviewing advance agreement proposals and audits of incurred costs.

Special allocations of IR&D/B&P costs are permitted from the home office to specific segments and from segment cost pools to specific final cost objectives provided the particular segment or final cost objectives would receive a disproportionate allocation of the costs under the prescribed allocation base. When a special allocation is used, it must be described in the contractor's disclosure statement. Where a disclosure statement is required, assure that it describes the special allocation and the circumstances which require it. The standard provides that any work performed by one segment for another segment shall not be treated as IR&D or B&P costs of the performing segment unless the work is part of an IR&D or B&P project of the performing segment (420.50(d)). If the work of the performing segment does not qualify as IR&D or B&P effort, the costs, including business unit general and administrative expenses, are transferred directly to the receiving segment. Auditors at the performing segment will be primarily responsible for reviewing the propriety of the accounting treatment of these interdivisional costs.

Following are pertinent illustrations of this standard's application.

- o A contractor currently uses a total cost input base to allocate G&A expense. In implementing CAS 420, the contractor proposes to exclude purchased services and major subcontracts from the allocation base for IR&D/B&P costs, citing the special allocation provisions of 420.50(f)(2). This practice would not comply with the standard. Allocation of IR&D/B&P costs to final cost objectives is to be on the same allocation bases used for G&A. Special allocations for classes of contracts (e.g., exclusions of major subcontracts from the base) are not appropriate under 420.50(f)(2). The special allocation provision in 420.50(f)(2) is limited to circumstances of a particular final cost objective.

This situation is common. Many contractors will argue that IR&D benefits in-house activity, rather than the work of subcontractors and vendors. Accordingly, they feel that material and subcontract costs should be excluded from the allocation base. To include them in the base may distort the results. The standard does not allow this latitude.

- o A contractor charges an engineering department's typing services for

proposal preparation direct to B&P projects. General support typing services applicable to B&P and other departmental effort are not separately identified but are charged to an intermediate overhead pool and allocated to B&P projects, contract engineering projects, and other cost objectives based on labor hours. The contractor's practice of charging general support B&P typing services to an intermediate overhead pool complies with CAS 420.50(a)(i). The B&P general support typing effort is not separately identified and classified as B&P cost and is not construed as being incurred "in like circumstances for a final cost objective" (420.50(a)). Therefore, B&P general support typing effort is allocable to an overhead account, providing the allocation practice is otherwise considered acceptable and equitable.

- o A company has eight segments. Segment A performs IR&D projects which have technical application to it and two other segments. Technical application is not identifiable to the remaining five segments. The cost of those projects performed by Segment A is transferred to the home office and allocated in equal parts (one-third) to the three segments. This practice complies with 420.50(e)(1) and 420.50(f)(1) providing the three segments receive equal technical applications. If an allocation of equal shares does not reflect the participation in technical applications, other allocation bases that could be considered include total cost input (for the three segments) or a base consisting of the same components used to allocate home office residual expenses.

CHAPTER 19OTHER CONTRACT AUDITSA. SCOPE OF CHAPTER

This chapter provides guidance for several other types of contract audits that OA auditors may sometimes be asked to perform. They are:

- o Audit of Preestablished Forward Pricing Factors,
- o Financial Capability Survey,
- o Audits in Connection With Contract Termination,
- o Post Award Review of Certified Cost or Pricing Data (Defective Pricing Review),
- o Advance Payments or Letter of Credit,
- o Review of Progress Payments, and
- o Rate Verification

B. AUDIT OF PREESTABLISHED FORWARD PRICING FACTORS

When a contractor will likely submit a large number of pricing proposals to the Government during a year, it may be appropriate to agree in advance on certain cost factors to be used, for a specified period, rather than to develop and audit the cost factors anew for each proposal. The cost factors to be covered by advance agreement may include the various indirect cost rates applied to Government work, labor hour rates, material and labor variances, and allowances for scrap and obsolescence.

The feasibility of using preestablished cost factors in forward pricing depends on several factors, including (1) the stability of the contractor's business volume and mix of work, (2) the stability of the contractor's organization, work force, and facilities used, and (3) the reliability of the cost accounting system and the system of internal controls. An advance agreement may be reached on only some of the cost factors cited above because of inherent concerns about the reliability of accounting records or operational volatility. But generally, the advantages of preestablished cost factors for forward pricing outweigh the disadvantages, and every means should be used to overcome existing concerns. Whatever the actual outcome, forward pricing rates are provisional and should be revised when circumstances change.

When the Government and the contractor agree to use this procedure, the contractor will prepare a separate submission of cost or pricing data covering all aspects of the cost factors for which rates are to be preestablished. Generally, preestablished cost factors should be effective for not more than a

year. When preestablished rates are necessary for one or more succeeding years to aid in pricing multi-year contract proposals, the rates should be developed separately for each year.

1. Purpose of Audit. Cost or pricing data submitted in support of proposed forward pricing factors are audited to ascertain if the data are accurate, complete, and current for negotiating preestablished rates.

2. Estimated Indirect Cost Rates. Estimated indirect cost rates are extremely important in the pricing and administration of contracts and subcontracts. They are used to price proposals and to facilitate provisional payment of indirect costs on cost-reimbursable contracts and subcontracts, pending the determination of actual indirect expense rates. All of an auditor's knowledge about a contractor's activities is used to review a proposal of estimated indirect cost rates.

a. Proposal Required - A proposal supporting the estimated indirect cost rates for the ensuing fiscal year or years must be complete. The proposal should explain (1) what aspects of the estimates are based on historical costs; (2) how future operations, likely future events, and economic forecasts were factored into the estimates; (3) planned accounting policy changes and their impact; and (4) any other factors or conditions which affected the development of the estimates. Where this information is complete, evaluate whether the data were properly applied in the circumstances. In any event, the auditor should make trend comparisons of the estimated costs and rates with prior years and current experience. Evaluate the impact of nonrecurring events, if the historical data include the related costs.

b. Cost Accounting Changes - Determine whether any cost accounting changes have been made since the last audit was completed, particularly if costs have been reclassified from direct to indirect, and vice versa, and if departments have been reassigned to different indirect expense pools. Where there is a significant change in volume contemplated from the prior period, either up or down, ascertain whether variable indirect costs show a corresponding change, and, if not, why not. Review indirect expenses of a non-variable nature which show significant variations between historical and proposed future estimated costs.

c. Unallowable Cost - Ascertain whether unallowable costs have been excluded from the indirect cost pool but included as part of the allocation base. Assure that the indirect cost pools do not include costs recovered through application of loading factors to another base.

d. Business Volume - If business volume is expected to decline, causing indirect cost rates to climb, the Government's financial exposure on cost-reimbursable contracts and subcontracts can be limited by negotiating a ceiling on the indirect cost rates. Such a recommendation should be made, where appropriate.

3. Labor Hour Rates. Labor hour rate proposals can contain subtle biases which, if not discovered, can benefit the contractor. The following audit steps are designed to establish the validity of proposed labor hour rates based on individual job classifications. If the contractor's proposal

is presented along other lines the steps should be modified to meet the situation.

- o Determine whether all employees presently assigned to a job classification are included in the listing used to compute the average hourly rate.
- o Determine the authorized straight time compensation range of each classification. Calculate the mean and median straight time rate of present employees in each classification.
- o Compare the straight time rates of listed individuals to approved personnel actions. Examine the justification for individuals paid more than the ceiling rate for the assigned classification.
- o Ascertain at what rates employees are hired (for example, lowest half of rate range, or not above median, etc.). Review turnover experience for possible effect on the mean and median rates.

If wage or salary escalation is built into the contractor's proposal, ascertain whether increases due to merit and increased productivity are calculated separately from increases based on forecasts or other labor market factors. Ascertain whether the factor for merit increases is in line with prior periods' experience and is based on company-wide planning and budget forecasts. Determine whether an inflation factor was used in company planning and budget forecasts and whether it is in line with general economic forecasts. If wage escalation is based on wage agreements, verify that the proposed increase conforms to the terms of the agreement. If the contractor has any contracts with an economic price adjustment clause, it may be that the labor hour rates should be priced without escalation for inflation. This procedure is particularly relevant in multi-year contracts.

4. Payroll Taxes and Fringe Benefits Rates. Use the following steps as a guide.

a. Payroll Taxes - Verify that the proposed payroll tax rates are those that will apply in the coming year and that, in the case of FICA and unemployment insurance, the rates have been factored down for the untaxable portion of annual salaries and wages.

b. Fringe Benefits - Examine the fringe benefit rate calculation for conformance to established plans and agreements. Ascertain whether rates applied are current and whether they reflect consideration of prospective rate changes.

5. Scrap, Spoilage, and Obsolescence Factors. Use the following steps as a guide.

a. Scrap and Spoilage - Determine if the proposed percentage factors for scrap and salvage are based on actual experience under recent production orders and if the factors recognize improvements in production techniques. If this experience has not been considered, develop a trend line of past production experience through use of graphic analysis (scatter diagram) and compute a scrap and salvage factor based on the trend. A scatter

diagram displays the relationship between two variables. In this case, the variables are the raw material placed into production and the scrap generated during production of various groups of units over time.

b. Obsolescence - Determine whether the proposed percentage factor for material obsolescence considers the state of development of the product being acquired and the likely reduction in the number of engineering changes which tend to create obsolete material. An obsolescence factor based on past faulty procurement practices or inadequate inventory records should not be accepted. The contractor should be required to improve its procedures and practices and to develop an obsolescence factor commensurate with efficient practices.

6. Standard Cost Variance. Standard costing is poorly suited for pricing items not in continuous production or for pricing items produced under special production units. If standards have been revised to approximate expected actual costs, no variance should be applied. If standards were revised in some other respect, the variances likely will also need revision so that the result will still approximate expected actual cost.

- o Where standard costs are used in estimating Government contract costs, determine whether they are segregated by product line to facilitate pricing of product orders.
- o If proposed standards are unchanged, determine whether application of the variance to the standard cost reasonably approximates expected actual cost, taking into consideration the effect of projected changes in volume and other operational considerations.

7. Reporting. The report format for audit of indirect cost rates, illustrated in exhibit A, chapter 17 (A:AM17EXA.WPF) should be adapted to report the results of audits of preestablished forward pricing factors.

C. FINANCIAL CAPABILITY SURVEY

A contracting official may request an auditor to ascertain whether a responsive bidder has the financial resources necessary to finance the stated work. This situation could occur when financial information, such as a balance sheet and income statement, submitted as part of a bid or proposal, raises questions about the adequacy of a company's cash flow and its credit rating. A preaward audit might also raise questions about a proposer's financial resources, leading to a financial capability survey. Frequently, a financial capability review is requested as a part of a preaward audit request.

1. Priority. Since award of a contract or subcontract depends on the outcome of this review, it carries a high priority rating, at least equivalent to that of a preaward audit of cost or pricing data.

2. Scope. The survey consists of two parts:

- o An evaluation of a prospective contractor's cash flow projections and underlying assumptions and, based on the results,

- o A determination as to whether the projected cash flow is sufficient to meet all financial requirements during the proposed contract period, taking into consideration the method and timing of payments contemplated on the contract under consideration for award.

3. General Guidance. A cash flow forecast developed specifically for Government contracting officials to demonstrate financial capability to obtain a contract award should be compared to internal cash flow forecasts developed for budgeting and planning purposes or for bank financing.

Cash flow projections need to be developed by month or by quarter so that projected changes in inventory levels, facilities, or staffing are fully and currently reflected in the forecast of disbursements.

4. Audit Procedures. The following audit steps are suggested for a financial capability audit.

- o Examine financial statements to determine cash and working capital trends. Compute the current and acid test ratios of the past few years to discern trends in the contractor's current position.
- o Review the cash balance per books and on the bank statements at various intervals throughout the past year, taking into account funds borrowed for short periods (as working capital).
- o Compare cash balance history with current projections. Assess the cash impact of projected changes in the mix of business or total sales and of business decisions regarding expansion.
- o Compare collection experience for trade receivables and Government contracts with current cash flow forecasts, taking into account any changes in the methods of payment employed on Government contracts between the periods under consideration.
- o Compare sales forecasts with production schedules and with production and sales of prior periods.
- o Verify projections of other income, e.g., dividends, interest, sale of investments, or sale of equipment.
- o Examine minutes of board of directors and other management meetings, as well as loan agreements, for clues to cash resources, limitations on use of existing resources, or management decisions that could effect cash resources.
- o Compare projected disbursements with historical data, taking into account projected changes in staffing, facilities employed, inventory levels, etc.
- o Verify projection of non-routine disbursements, e.g., major equipment acquisition or repayment of loans.

5. Reporting. A standard format is not prescribed for reporting the results of a financial capability survey. Since contracting officials are

probably awaiting the results of the survey, the audit results may be conveyed verbally as soon as the field work has been completed and factual matters have been discussed with the prospective contractor. See exhibit B, chapter 15 (A:AM15EXB.WPF) for an example of how the audit results are incorporated into a preaward audit report.

D. AUDITS IN CONNECTION WITH CONTRACT TERMINATION

This section describes audit procedures for reviewing cost submissions under contracts and subcontracts which have been partially or fully terminated prior to completion. A termination may be at the Government's convenience or for default. The cause for termination and the type of contract involved are important factors in determining the auditing requirements. Contract cost principles applicable to termination costs are found in FAR 31.205-42, 49.2, and 49.3.

1. Partial or Complete Termination of Fixed Price Contracts for Convenience. Settlement proposals covering partial or complete termination of a fixed price contract for convenience can require considerable audit effort.

Extensive familiarity with the contractor's cost accounting system, underlying internal controls, and the contractor's operations is helpful in auditing fixed price termination settlement proposals. The contractor's objective in developing a settlement proposal is different from the objective of a pricing proposal or a summary of incurred costs. The contractor is intent on being wholly compensated for assumed risks on a contract that will not be completed.

To determine the audit scope, it is important to thoroughly review the settlement proposal and underlying support, the termination notice, pertinent contract provisions, the original pricing proposal, related cost or pricing data, and the job cost history of the terminated work.

For production contracts, a key element in any termination audit is the verification and pricing of the inventory of raw materials, work in process, and finished goods. Following are specific audit considerations applying to the examination of inventories.

a. Claim Submitted on the Inventory Basis - The Government prefers that settlement proposals for fixed-price contracts be submitted on the inventory basis. This basis requires that the cost elements and profit included in the settlement proposal be directly associated with the physical units or services which were terminated. It limits the claim to those items which are residual as a result of the termination action. The claim is made using SF-1435 (Settlement Proposal, Inventory Basis). The auditor should verify that the claim includes only items allowable to the terminated portion of the contract. Guidance for reviewing the various classes of inventory items follows:

(1) Raw Materials Inventory. Raw materials, metals, purchased parts, and supplies in inventory represent items not placed into production. Assure that no direct labor or overhead, other than material handling, is included in the inventory cost. Compare the quantities and pricing of the inventory items to supporting bills of materials, cost records,

invoices, and purchase orders. Review any material handling charges for conformance to regular practices. Determine if the inventory was screened for items returnable to suppliers and items usable on other work (with full credit to the contract). Determine whether the scrap value of the inventory has been established.

(2) Work-in-Process and Finished Components. Finished components and work-in-process inventory have had value added to the basic raw materials, metals, purchased parts, and supplies through some form of fabrication or processing. The audit objective is to verify the types and quantities of items in the inventory and the basis used to price them.

(a) Work-in-Process. Review available cost data, cost reports, cost standards, engineering and bid estimates, bills of material, and other information related to the cost of operations to establish the reliability and accuracy of the prices shown. Determine whether the inventory was screened for items usable on other work without loss to the contractor.

(b) Finished Components. Where undelivered finished products are listed, ascertain whether the contract prices have been adjusted to consider savings on freight charges. Verify all adjustments made to contract prices. If rework is necessary to make completed items acceptable, the estimated rework costs should be credited against the contract price.

(3) Miscellaneous Inventory. Miscellaneous inventory includes items which do not fit into the foregoing categories. The costs claimed for miscellaneous inventory should be limited to material cost and any applicable handling charges. Determine if the inventory was also screened for use by the contractor (without loss) or for return to suppliers.

b. Claim Submitted on the Total Cost Basis - Use of the total cost basis for submission of a termination claim is allowed only when approved in advance by contracting officials. The claim is made using SF-1436 (Settlement Proposal, Total Cost Basis). A claim on the total cost basis itemizes costs by cost element up to the time of termination plus settlement expenses and profit, less the contract price for delivered items. All unliquidated advances, progress payments, and disposal and other credits known when the proposal is submitted should also be deducted. Because of the manner in which this form is prepared, a claim related to a partial termination is not submitted until the continued portion of the contract has been completed.

Costs for the entire contract should be reviewed using guidance provided in chapter 16, Incurred Cost Audits. Also, since the costs of the residual inventory are included in the audited costs, it is important to determine whether inventory schedules are accurate, complete, and current from a standpoint of quantity and allowability to the terminated work. Test physical counts of items following the applicable guidelines provided in the following paragraphs.

c. Further Verification of Residual Inventories - The cost of residual materials made obsolete by a negotiated change to the contract is not allowable as termination inventory.

(1) Quantities. Determine whether the residual quantities of major items are reasonable by comparing them (1) with the bill of materials used to determine contract prices and (2) with quantities purchased less quantities placed in production, taking into account scrap and spoilage factors. Ascertain whether any items in the residual inventory were purchased prior to the current contract. The cost of such items should generally not be allowed. Ascertain whether the quantities of items in inventory are greater than are necessary to satisfy contract requirements.

(2) Rejects. If the residual inventory includes rejects that can be reworked and made into acceptable finished products, determine that they are priced at the contract price less the estimated cost of rework and listed with the finished goods.

d. Special Tooling, Machinery, and Equipment - Consideration of any claim for loss on these types of items largely depends on the intent of the negotiating parties. Where cost or pricing data used in establishing contract prices provided for these items to be paid for as part of the product prices, it may be feasible to prorate the costs between completed work and terminated work. Still, as with material inventory, first establish that the items were not acquired prior to the contract and are not usable on other work.

e. Initial Costs - Initial costs include nonrecurring preparatory costs, engineering costs, etc., which are seldom segregated in the accounts but which may have been itemized in the original pricing proposal. Review the cost elements claimed and the underlying support, and compare the data to the initial cost or pricing data estimates to ascertain reasonableness of the costs claimed. Remember that only the initial costs that are allowable to the terminated portion of the contract can be included in the settlement proposal.

(1) Starting Load Cost. Initial costs may also include starting load costs or higher than average unit costs of early production. If production is costed in reasonably small lots, it may be relatively easy for the contractor to develop information about material losses and labor inefficiency in the early stages of the contract work. If these costs cannot be traced through lot work orders, attempt to verify claimed amounts using scrap reports, spoilage tickets, labor efficiency reports, production records, and labor distribution records.

(2) Direct Labor. For direct labor, a learning curve analysis may be used to estimate the initial costs allocable to the terminated portion of the work. If available, the contractor's normal rate of learning may be used to project what the total direct labor hours would have been, had the contract been completed. The average direct labor hours per unit can then be determined and applied to the delivered units. Deduct those hours from the total hours required to produce the delivered units. The difference can then be priced using historical labor and indirect cost rates. Caution must be exercised when using this procedure, because such factors as contract modifications, engineering changes, and other abnormalities can contaminate the raw data.

(3) Engineering Costs. If unrecovered engineering costs are claimed, assure that the effort represented by the claimed costs was intended

to be recovered evenly over the units originally contracted for and not as a separate item under the contract. Also, assure that the engineering effort was completed. If it was completed and the contract was completely terminated, the cost may be properly allocable to the termination. However, under a partial termination, where there is a continuing portion of the contract, engineering costs should not be allocated to the terminated portion of the contract.

f. Severance Pay - In considering whether a claim for abnormal severance is allowable and allocable as a direct charge, determine (1) the extent of effort needed to keep severance pay to a minimum by reassigning terminated employees to other work and not hiring from outside the company, (2) the period in which the severance pay was earned compared to the period of contract work, (3) whether severance pay was computed correctly, and (4) the effect it may have on normal severance reserves, pension costs (including generating significant reversionary credits), etc.

g. Rental Costs Under Unexpired Leases - Determine whether the contractor has made all reasonable efforts to reduce the cost of any unexpired leases. Also determine if the amount claimed represents reasonable rent for the period of anticipated contract performance.

h. Travel Costs - In limited circumstances, travel costs can be claimed as allocable to the terminated portion of the contract. Consequently, care must be exercised to determine if claimed travel costs benefited the entire contract, or just the delivered items. Travel costs incurred for termination activities should be included with settlement expenses. If included elsewhere, an audit adjustment should be made.

i. Costs After Termination - For costs claimed that were incurred after the effective date of the termination (and are not part of settlement expenses), determine if the action to incur the costs was not just to increase costs and/or profit recoverable in the claim.

Where unabsorbed overhead applying to the period following termination is claimed, it should be classified as unallowable. The only overhead allowed as a direct charge after termination pertains to abnormal type costs, such as mass severance pay.

j. Subcontracts - In general, subcontract settlements should follow the same principles as prime contracts. The prime contractor is responsible for settling subcontractors' termination claims.

(1) Review of Claim. Review subcontract settlements for reasonableness and conformance with subcontract terms and applicable regulations. Assure that the contracting officer has approved settlements exceeding the threshold amount prescribed in FAR 49.108-4. The prime contractor may complete settlements involving less than this threshold amount based on the contracting official's written authorization and without ratification or post-approval.

(2) Reporting. If the audits of subcontract settlement claims are incomplete when the audit report is being prepared, the claimed costs

should be classified as unresolved, and the reason for this classification explained in a footnote.

k. Settlement Expenses - Settlement expenses are costs which are incurred as a direct result of termination. They should be collected under a separate job order, if significant. Profit is not earned on settlement expenses. Therefore, assure that settlement expenses are distinguished from other costs applying to the terminated work.

Settlement expenses are frequently G&A type expenses. Assure that items claimed directly as settlement expenses are excluded from the G&A expense allocated to continuing contracts.

l. Evaluation of Profit/Adjustment for Loss - The claim should not include any amount for profit on the terminated work or on settlement expenses. Also, no profit is allowed if it appears that the contractor would have incurred a loss had the contract been completed. Where a loss is projected, the termination claim should be reduced by an amount equal to the pro rata portion of any loss that would have been sustained had the contract been completed.

To ascertain or verify the loss adjustment, the contractor must estimate the cost required to complete the terminated portion of the contract. This estimate is used in conjunction with the actual job cost history to determine whether a loss would have been incurred. The estimate to complete should be carefully reviewed and a technical evaluation requested, if necessary.

2. Equitable Adjustment Proposal. A claim for an equitable adjustment of the price of the continuing portion of the contract may result from a partial termination. The claim is submitted as cost or pricing data using SF-1411 and is audited as any preaward audit, taking into consideration the special circumstances posed by the termination. Claims submitted for equitable adjustments must be filed prior to settlement of the terminated portion of the contract.

a. Basis for Claim - Equitable adjustments are permitted to enable the contractor to recover higher per unit costs occasioned by the decrease in the number of deliverable end units. Higher per unit material costs may be incurred, because quantity discounts will not be obtained, and per unit direct labor costs will be higher when anticipated labor efficiency improvements will not be realized. Also, starting load costs will be allocated over a smaller number of units.

b. Unabsorbed Overhead - Contractors have, on occasion, claimed unabsorbed overhead in termination settlement proposals. Unabsorbed overhead represents indirect expenses which the terminated contract (or terminated portion of the contract) would have absorbed and which, because of the termination, must be allocated to other work. All claims for unabsorbed overhead, however represented, will be questioned. The Armed Services Board of Contract Appeals has held that unabsorbed overhead is not a bona-fide continuing cost of a terminated contract.

3. Complete Termination of a Cost-type Contract for Convenience.

Contractors have two options for claiming costs after the termination date, as outlined below.

a. SF-1034 - A contractor can elect to use SF-1034, Public Voucher for Purchases and Services Other than Personal, to claim costs for 6 months after the effective termination date. The guidance provided in chapter 16 applies as well to the audit of costs invoiced up to the time the final SF-1034 is submitted. However, judging the reasonableness of costs incurred following notice of termination includes considering the steps taken to stop work promptly, terminate subcontracts and purchase orders, reassign or dismiss persons who were dedicated to the terminated work, and to otherwise reduce the continuing costs of terminated work.

b. SF-1437 - The contractor can also elect to stop submitting the SF-1034 Public Voucher at any time in the 6 month period. Any unvouchered costs (and proposed additional fee) can be included in the final settlement proposal (SF-1437). This settlement proposal must be submitted within 1 year of the effective date of termination, unless contracting officials extend the period. The audit of the settlement proposal should be conducted similarly to that described above for the post-termination vouchers. Assure that the settlement proposal does not contain any previously vouchered costs.

4. Partial Termination of a Cost-Type Contract for Convenience.

Generally, the settlement adjustment of a partial termination of a costtype contract for convenience only concerns fee adjustment. This adjustment would not require audit involvement unless contracting officials want audit assistance in verifying the physical percentage of completion of the terminated work and the cost incurred for that segment of work.

5. Termination of a Cost-Reimbursement Contract for Default. The supplementary cost principles applicable to terminations of costreimbursement contracts for convenience also apply to default terminations except that (1) the costs of preparing the settlement proposals are not allowable and (2) while allowable costs are reimbursed, an appropriate reduction is made in the total fee. Also, a cost-reimbursement contract does not contain any provision for recovering excess repurchase costs after termination for default, as fixed price contracts do.

6. Termination of a Fixed-Price Contract for Default. Under a termination for default, the Government is not liable for the contractor's cost of undelivered work and is entitled to the repayment of advance and progress payments, if any, applicable to that work. A contractor held in default is also liable for any excess costs incurred if the Government repurchases the terminated supplies or services. Audit services are usually not required in the event of termination of a fixed-price contract for default.

7. Reporting. An audit report covering a termination claim audit should be prepared according to the format prescribed in the model report in exhibit A (A:AM19EXA.WPF). An audit report covering review of an equitable adjustment proposal should be prepared according to the format prescribed in the model report in exhibit B (A:AM19EXB.WPF).

E. POST AWARD REVIEW OF CERTIFIED COST OR PRICING DATA (DEFECTIVE PRICING REVIEW)

The Truth in Negotiations Act, enacted as Public Law 87-653 in 1962, requires prime contractors and subcontractors, under certain circumstances (shown in FAR 15.804), to submit and certify cost or pricing data supporting proposed prices. The Act further provides for the contract price to be adjusted when such certified data are found to be inaccurate, incomplete, or noncurrent as of the date of the final agreement on price.

1. Purpose of a Post Award Review. A post award review of certified cost or pricing data is made to ascertain whether data relied upon in contract negotiations were accurate, complete, or current as of the date of the final agreement on price and whether reliance on any inaccurate, incomplete, or noncurrent data increased the contract price significantly. This type of audit is commonly known as a defective pricing review.

Cost or pricing data are defined in FAR 15.801. Such data include "all facts as of the time of price agreement that prudent buyers and sellers would reasonably expect to affect price negotiations significantly." The important points to remember are that cost or pricing data (1) involve only facts, as opposed to judgments (e.g., contractor estimates of future overhead rates) and (2) are not limited to data furnished in support of the proposal; they also include all factual data that were reasonably available to the contractor as of the date of certification. Another important point to bear in mind is that the Contracting Officer must have relied on the data furnished by the contractor when negotiating the contract price. If defective data furnished by the contractor were not relied upon, defective pricing cannot be charged. Also, a contractor's failure to certify submitted cost or pricing data, as required by a contract, does not preclude the Government from claiming that the data were defective. The Armed Services Board of Contract Appeals so stated in S.T. Research Corporation, ASBCA No. 29070;84-3 BCA, paragraph 17,568. Therefore, defective pricing reviews of selected contracts can be accomplished whenever the contract includes the required cost or pricing data clause, whether or not the contractor executed a certification.

2. Responsibilities. The DAIG/AO has overall responsibility for monitoring the defective pricing audit program within OA. The DAIG/AO will coordinate with DCAA Headquarters any matters relating to defective pricing at the Headquarters level.

The DAIG/AP³ will, as part of the annual program guidance, include staff days for defective pricing audits based on historical experience. Regional Managers will have responsibility for obtaining listings of subcontracts containing defective pricing clauses from their respective field offices; making judgmental selection of contracts to be reviewed; and performing or arranging for defective pricing audits. Regional Managers are to budget adequate time and resources to accomplish these audits.

3. Developing the Audit Universe. The Office of Procurement and Assistance Management has agreed to furnish to the OIG listings of DOE fixed-price actions (basic contracts and modifications) over \$500,000

containing the defective pricing clause. Capital Region will make this request, arrange to have the listings segregated by geographic area of OIG responsibility, and provide appropriate listings to the Regional Managers.

For subcontracts, Regional Managers will annually request from each of the field offices within their geographic area of audit cognizance a listing of all fixed-price actions (basic contracts and modifications) over \$500,000 containing the defective pricing clause. These listings should be obtained within 90 days of the end of the fiscal year.

The requests for listings should include an invitation to procurement officials to request defective pricing audits on specific contracts which they suspect may contain defective pricing.

4. Selection Criteria. AO's objective is to schedule an adequate number of defective pricing reviews to assure that DOE contractors are in compliance with regulations regarding cost or pricing data. Contracts selected for review should first be screened to ensure that they contain the defective pricing clause.

a. Contracts Over \$1 Million - Contracts included in the listings furnished to the OIG which exceed \$1 million will be stratified according to dollar value. Selection will be made for postaward review giving priority to highest dollar value contracts based on available budgetary resources for the use of DCAA and IPA's. While it is desirable that all fixed-price contracts over \$1 million containing the defective pricing clause be reviewed, budgetary constraints may preclude full coverage. Therefore, a dollar stratification together with those factors described below should be used in selecting contracts for review.

b. Contracts Between \$500,000 and \$1 Million - A small sample of contracts included in the listings furnished to the OIG which range between \$500,000 and \$1 million should be reviewed. Normally, between three and five such contracts should be selected for review in each region. Factors to be considered in the selection should include the contractor's prior history of defective pricing and relevant input from procurement officials.

5. Determining Cognizant Audit Agency. For those contracts selected for review, a determination will first be made whether DCAA is the cognizant audit agency. Reference can be made to the Directory of DCAA offices or the DCAA field office located in the vicinity of the contractor can be called on the telephone. In the event that DCAA is not cognizant, the OIG cognizant region will determine how these audits will be performed, and by whom.

6. Assigning or Requesting Defective Pricing Reviews. When the contracts selected for review fall within the selecting region's area of cognizance, the Regional Manager will make arrangements for the audit, consulting DCAA as appropriate. If a selected contract falls within the cognizance of another Regional Office, a request for audit assistance should be made to the cognizant Regional Manager.

In the event that several contracts are selected for review at the same contractor location, the request for audit assistance should state that the audit may be curtailed if no apparent defective pricing is found in half of

the contracts selected for review at that location. However, the request for audit assistance should state that summary cost data must be reviewed on all selected contracts to determine if there were significant underruns in any cost element (labor, materials, etc.) and that followup should be made to determine whether such underruns were due to defective pricing.

7. Monitoring. Regional Managers will be responsible for monitoring the quality and timeliness of postaward audits for defective pricing performed within their regions. In this regard, any unresolved problems arising with DCAA in connection with requested defective pricing audits should be referred to the DAIG/AO for resolution with DCAA Headquarters.

8. Reporting on Defective Pricing Audit Activity. Within 30 days after the end of each calendar quarter, OIG Regional Managers will submit a report of defective pricing activity to the DAIG/AO. The report will contain, as a minimum, the following information for each defective pricing report issued or received from DCAA in that quarter:

- o Contractor's name and location.
- o Number of contracts audited.
- o Number of contracts containing apparent defective pricing.
- o Total dollar value of contracts audited.
- o Total dollar amount of identified defective pricing.

In addition to the above, Regional Managers are encouraged to include in their report any other items of interest, such as contracting officer action on prior defective pricing reports.

9. Timing of Post Award Audit. A post award audit can be performed until 3 years after final payment of the contract. However, the reviews should be made before the contract is physically completed, since the related cost or pricing data and contractor individuals who prepared the proposal are readily available then. Many auditors believe that the audit can be performed effectively after most of the materials have been procured, and the work has progressed to the point where labor cost trends can be discerned.

10. Audit Steps. Suggested audit steps for defective pricing audits include the following.

a. General - Examine both auditor and Contracting Officer files, obtain and review contractor's price proposal, related preaward audit report, certificate of current cost and pricing data, procurement negotiation memorandum, and Government technical reports, if available. Note whether (a) the contractor's submitted cost or pricing data were relied on, (b) there was a significant delay between the time the proposal was prepared and the certificate was executed (if there was, the proposal should have been updated with more current data, and (c) the preaward audit report shows large amounts of unsupported costs.

If the contract is completed or nearly completed, compare total costs incurred to the certified proposed costs. If the results show a substantial overrun, terminating the audit should be considered. On the other hand, if an underrun is apparent, compare individual cost elements to identify the area(s) accounting for the underrun. Perform some or all of the following steps depending on the area(s) identified.

b. Direct Labor. Suggested audit steps for direct labor include the following.

1. If proposed labor hours were judgmental (engineering estimate) and no related historical data were available, detailed review of this area may not be necessary. However, if the hours are based on historical data, determine whether the data used were accurate, current, and complete up to the point of certification. If experience data were available and were not used, obtain reasons why they were not. Compare the historical data with those proposed.

2. Compare actual labor rates with the proposed rates. Ascertain whether the latest rates available were used in pricing the hours; consider the contents of the latest union agreement or projected wage increases, including cost of living adjustments.

c. Direct Materials. Suggested audit steps covering direct materials are listed below.

On a test basis, examine material purchases and compare prices paid with the pricing information in the original proposal. Where the actual prices paid were lower, determine whether this pricing information was known prior to the agreement on contract price but was withheld from the Government.

For significant items, ascertain whether the quantity purchased was less than the proposed quantity. If engineering improvements made this change possible, ascertain whether this knowledge was developed prior to the agreement on contract price. If actual scrap and spoilage is substantially different than estimated in the proposal, review the information provided in the proposal and the production history of other similar work to ascertain whether the proposed scrap and spoilage factors were correctly determined.

Ascertain whether actual production and procurement conformed to the make-or-buy decisions in the pricing proposal. Where changes occurred, inquire into the reasons and examine data showing comparative costs. Where the actual cost is less than that proposed, determine whether the information provided during audit and during negotiations about make-or-buy decisions was accurate, complete, and current at that time.

Determine whether the accounting treatment of purchased materials was consistent with the classification of direct materials in the pricing proposal.

d. Subcontracts. Compare actual subcontract prices and other pertinent information with information provided prior to agreement on the contract price. Where prices are less than those proposed to the Government, ascertain whether negotiations were completed at the time of final agreement

on contract price. Determine whether the contractor had developed negotiating objectives or "most probable outcome" for scheduled subcontract negotiations that differed from the prices quoted to the Government.

e. Other Direct Costs. Suggested audit steps concerning other direct costs are listed below.

Determine whether the accounting treatment of other direct costs is consistent with the types of costs so classified in the pricing proposal. Where costs are classified as indirect but were proposed as direct, recast the audited pricing proposal to reflect this fact and calculate the amount by which the contract price was overstated.

Where percentage factors were used in the proposal to apply certain types of costs to direct material or direct labor, determine whether the actual costs incurred approximate the proposed costs.

Compare other direct costs being incurred, by category, to proposed costs. Where actual costs are significantly less than the proposed amounts, determine whether there is any basis for judging the pricing proposal to be defective.

f. Indirect Costs. Suggested audit steps for indirect costs include the following.

Compare proposed rates, by year if proposed in that manner, to actual rates. If the actual rates are significantly lower, determine the cause and consider whether it should have been known at time of certification and, therefore, disclosed.

Compare proposed indirect expense bases, as well as expenses, to the latest available forecasts/budgets at time of certification. A substantial increase in volume could cause indirect expense rates to drop. If this increase was anticipated at time of certification, it should have been disclosed. Also, differences in rates may be attributable to changes in the structure of overhead pools which were not considered when developing the proposed costs.

g. Offsetting Cost Overstatements Against Understatements. If the audit disclosed cost understatements which also were known but not factored into the final contract price, they may be set-off against the cost overstatements disclosed in the current examination. Note, however, that set-offs are permissible only within an individual pricing action and not between two or more pricing actions. (Refer to FAR 15.804-7(b)3.)

11. Reporting. A written report should be prepared on each post award audit of certified cost or pricing data, even if no defective pricing is found. Where defective pricing is found, the audited pricing proposal must be recast and the price overstatement computed. Should defective pricing be uncovered after an audit has been completed, the format in the DCAA contract audit manual (chapter 10-600) can be used as a guide with respect to report content modified to include the Yellow Book requirements for financial audits that are applicable.

F. ADVANCE PAYMENTS/LETTER OF CREDIT

Advance payments may be provided on any type of contract. Although this method of financing is not preferred, it is considered acceptable in the following situations (FAR 32.403):

- o Agreements with non-profit educational or research institutions for experimental, developmental, or research work;
- o Contracts solely for managing and operating Government-owned plants;
- o Contracts for acquiring facilities, at cost, for Government ownership;
- o Contracts involving operations so remote from a financial institution that the financial institution could not be expected to provide suitable administration of a guaranteed loan;
- o Contracts of such a highly classified nature that the agency considers it undesirable for national security reasons to permit assignment of claims under the contract;
- o Rare but essential contracts with unusually weak or financially overextended contractors, in which performance may be improved and risks of financial loss minimized by close control of funds;
- o Contracts for which a guaranteed loan would result in exorbitant interest rates; and
- o Exceptional cases where advance payments are more beneficial to the Government than any other available method of financing.

When advances for contract work are not expected to exceed the amount asserted in FAR 32.406(b)(1), or where a long-term contract relationship is not envisioned, advance payment may be made by treasury check. Where a continuing contract relationship is envisioned and advances will total more than the established threshold, a letter of credit must be authorized for advance payment of contract costs. In either case, the Government wants to reduce the elapsed time between receipt of the advance and disbursement of the funds in order to minimize idle Government funds in commercial banks.

Advance payments must be deposited in a special bank account covered by a special agreement to protect the Government's interests. According to FAR, funds are withdrawn from a special bank account under the letter of credit financing approach in one of two ways.

- o Checks Paid - Drawdown on the letter of credit is delayed until the disbursement checks issued by the recipient are presented to the contractor's bank for payment.
- o Delay of Drawdown - Drawdown is delayed until after disbursement checks issued by the contractor organization have been forwarded to the payees.

Some contractors may still be operating under earlier FAR provisions where future disbursements are estimated and drawdowns are made as close as possible to the time funds are required.

1. Scope of Audit. Under the letter of credit method of financing, much of the responsibility for financial administration is shifted to the contractor and withdrawal of Government funds can be better timed to coincide with cash needs. Periodic examination is necessary to determine if cash management and monitoring practices of letter of credit funds are adequate to ensure proper accounting for and physical security of funds and that cash balances are kept to the minimum amount necessary to satisfy immediate payment needs.

Where deemed necessary, special bank accounts used for direct treasury check advances can be similarly examined. The audit steps below apply equally to this method of advance financing of contracts.

2. Audit Procedures. The scope of an audit of special bank account activity and balances should follow generally recognized and accepted auditing procedures, appropriate under the circumstances. Audit procedures should include:

- o Direct confirmation of the special bank account balance;
- o Reconciliation of the confirmed bank balance with the contractor's records and, for letters of credit, with the most recent statement of accountability of funds furnished the Government;
- o Proof of the disbursement and deposit transactions shown on bank statements with the contractor's records;
- o Review and evaluation of the use of the funds to insure propriety;
- o Verification that Government advances are deposited promptly;
- o Verification that advances made to subcontractors are in accordance with basic agreements and are properly authorized and approved; and
- o Verification that the amount of the fund is not excessive considering the needs of the contractor to finance performance of the contract.

3. Reporting. A standard format is not prescribed for audits of advance payments, letters of credit, and special bank account activity. The written report should set forth the purpose, scope, results, and conclusion, according to professional standards of audit reporting, including Yellow Book requirements.

G. REVIEW OF PROGRESS PAYMENTS

Progress payments are usually authorized in supply contracts involving long production lead times requiring significant expenditures prior to

delivery. Progress payments based on costs are usually limited to a stated percentage of total cost. The payments are for work performed on the undelivered portions of the contract.

1. Scope of Audit. The amount of audit effort depends on the auditor's familiarity with the contractor's operation. Where the auditor has no prior experience with the contractor, a limited review of the contractor's accounting system and billing procedures should be performed to determine their reliability.

2. Audit Procedures. The audit procedures to be considered in reviewing progress payments include a determination that:

- o Costs claimed have been incurred or paid;
- o The sum of all unliquidated progress payments does not exceed contract limitations;
- o Obligations are paid on a current basis;
- o Overhead is based on acceptable rates;
- o The contractor's accounting system is adequate;
- o Payments are not duplicated when other types of financing are used;
- o The contractor accurately computes the cost of items delivered;
- o The contracting officer has approved the use of unusual progress payment rates;
- o Progress payments for first article costs do not exceed the applicable cost limitations where first article approval is contractually required;
- o Profit rates under alternative liquidation methods, where approved, do not exceed the contractor's actual profit rate;
- o Credit for disposal of property under the contract is current and accurate;
- o Each order under a basic ordering agreement is treated as a separate contract requiring separate cost accumulations; and
- o The prime contractor's review of subcontractor progress payment claims is satisfactory.

3. Reporting. A standard audit format is not prescribed for reviews of progress payments. The written report should set forth the purpose, scope, results, and conclusion, according to professional standards of audit reporting, including Yellow Book requirements.

H. RATE VERIFICATION

Verbal requests may be received for current, preestablished rates for indirect costs or other pricing factors. It is IG policy that contractor information be furnished only to Government personnel. If others request information under Government contracts, the contractor must be notified and asked for permission to release this information. The Regional Offices should keep a log of all verbal requests showing to whom and what information is given.

If rate information applying to the current period has been audited, the results can be used to reply to verbal requests. If the current pre-established forward pricing factors have not been audited there are several alternative courses of action. Proposed rates can be compared to audited data from prior periods and differences discussed with the contractor. Where accounting system changes have occurred since the last audit, it may be advisable to examine the effects and financial impacts of the changes before giving advice to the requester.

If there is no audit history on which to base a conclusion, it may be impossible to respond to the request without conducting an audit.

I. REVIEW OF INVOICES OR PUBLIC VOUCHERS

OA generally does not review the periodic invoices or public vouchers submitted by cost-type contractors as is customary with DCAA. A review of the billing system, including specific billing(s), may be performed by special request of the contracting officer and based upon suspected problems.

1. Purpose of Audit. The audit is made to ensure that invoiced amounts are consistent with contract terms and underlying regulations. Payments are provisional and are subject to retroactive adjustment based upon a detailed audit of costs performed at an interim point or upon contract completion.

2. Initial Review of Billing Procedures. For cost-reimbursable contracts with new contractors, review the billing procedures to determine whether amounts billed are reconciled monthly, by cost element, with job cost records. Through appropriate tests, verify the following for a specific billing(s):

- o The pricing of inventory issues billed;
- o That billings for inventory issues constitute issues for current use in the contract work, and not merely issues to an interim holding area made to facilitate reimbursement;
- o Payments for purchased materials;
- o That payments for materials and services are not delinquent;
- o That billed direct labor is based on recorded labor distribution job cost summaries;

- o That the job cost record properly supports other items of direct cost billed;
- o That adjustments to any item of billed costs are supported by properly approved, recorded journal vouchers; and
- o That overhead and G&A rates used in billing conform to rates agreed upon with contracting officials.

3. Reporting on Review of Billing Procedures. An audit report should be prepared explaining the results of the review and what costs are considered unacceptable for payment because of deficiencies in the contractor's billing system. The written report should set forth the purpose, scope, results, and conclusion, according to professional standards of audit reporting, including Yellow Book requirements. The format for an accounting system review should be used as appropriate to reflect the results (see chapter 18, exhibit D, A:AM18EXD.WPF).

EXAMPLE OF TERMINATION AUDIT REPORT

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITS

AUDIT OF
TERMINATION SETTLEMENT PROPOSAL
SUBCONTRACT NO. Q-1234-5678-T
ISSUED BY ABC, INC., UNDER
CONTRACT NO. DE-YZ-987654321
DEF CORPORATION
CITY, STATE

REPORT NUMBER:

PURPOSE AND SCOPE

In response to a request from the U.S. Department of Energy (DOE), Field Office, Chicago, we audited DEF Corporation's termination costs claimed for Task Agreement No. 90-U20 under Subcontract No. Q-12345678-T. ABC, Inc., was notified on March 14, 1988, that task agreements for the ... project office would be terminated for the convenience of the Government on April 30, 1988. DEF's settlement proposal submitted on November 12, 1988, consisted of settlement expenses of \$28,404 and a \$4,595 fee. DEF submitted a modification to this proposal on June 3, 1989, increasing settlement expenses by \$29,059.

The termination settlement proposal and related supporting data are the responsibility of the contractor. Our responsibility is to reach a conclusion on the termination settlement proposal based on our audit.

The purpose of the audit was to determine the allowability of costs claimed to use as a basis for negotiating a final settlement of the subcontract. Allowable costs are costs incurred that are reasonable, allocable, and in accordance with the terms of the subcontract, applicable cost principles, laws and regulations, and generally accepted accounting principles and practices appropriate to the particular circumstances.

The audit scope was limited to test procedures for validating DEF's claimed costs by tracing them to books of original entry and supporting records. We tested specific transactions, but did not evaluate DEF's total internal control system or technical aspects of its performance.

As defined in the above scope paragraph(s) we conducted our audit in accordance with generally accepted Government auditing standards that applied to this financial related audit. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the data and records reviewed are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records reviewed. An audit also includes assessing the accounting principles used and significant estimates made by the contractor, as well as evaluating the overall presentation. We used the terms and conditions of

the subcontract and applicable sections of the Federal Acquisition Regulations (FAR) and the DOE Acquisition Regulations (DEAR) as criteria in evaluating proposed termination costs. We believe that our audit provides a reasonable basis for our audit conclusions.

We completed our onsite work on August 15, 1989.

CIRCUMSTANCES AFFECTING THE AUDIT

We did not perform a technical review of the subcontract. Accordingly, audit results are qualified pending the outcome of such a review.

The Defense Contract Audit Agency (DCAA) audited DEF's indirect cost rates for 1988. The scope of our audit of indirect costs was limited to determining if the 1988 indirect costs claimed were based on DCAA's recommended final rates applied to the appropriate allocation bases. DCAA has not yet audited DEF's Fiscal Year (FY) 1989 indirect cost rates; accordingly we classified FY 1989 indirect costs as unresolved.

AUDIT RESULTS

As described in the notes to exhibit A, we questioned \$38,326 and classified \$7,220 as unresolved.

We conclude that, because of the questioned costs summarized above and described in the notes to exhibit A, the termination costs claimed do not represent a reasonable basis for negotiating a final subcontract settlement.

Compliance with applicable laws and regulations related to the subcontract is the responsibility of DEF management. As part of our evaluation, we performed tests of compliance with certain provisions of laws and regulations related to the subcontract. Our objective was not, however, to reach a conclusion on overall compliance with such provisions.

The results of our tests indicate that, for the items tested, DEF complied in all material respects with the provisions of applicable laws and regulations related to the subcontract. For the items not tested, nothing came to our attention that caused us to believe that DEF had not complied, in all material respects, with those provisions.

We discussed the audit results with DEF's president, on August 15, 1989.

OTHER MATTERS TO BE REPORTED

In planning and performing our audit of termination costs claimed by DEF under Subcontract No. Q-1234-5678-T, we considered its internal control structure to determine our auditing procedures for the purpose of reaching a conclusion on termination costs and not to provide assurance on the internal control structure.

DEF management is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The

objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit preparation of termination costs in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purposes of this report, we classified the significant internal control structure policies and procedures as those that relate to the recording and reporting of costs under Government subcontracts and to ensuring compliance with laws and regulations that have a material impact on termination costs claimed. These are control procedures designed to ensure that:

- o The breakdown of costs within the accounting system was adequate for cost determination purposes.
- o Specific cost elements were afforded consistent treatment regarding Government and non-Government cost objectives.
- o Allowable and unallowable costs were routinely identified and segregated in the accounting system.
- o Adequate source documentation supported all costs.
- o Assets were safeguarded against loss or unauthorized use or disposition.
- o All accounting data were accurate, reliable, and traceable to underlying source documentation.
- o Subcontract terms and conditions were known by appropriate personnel and the effects of subcontract terms and conditions were properly reflected in the accounting records.

For the internal control categories listed above, we obtained an understanding of the design of relevant policies and procedures, determined if they had been placed in operation, and assessed control risk.

We noted certain matters involving the internal control structure and its operation that we consider reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions are matters coming to our attention relating to significant deficiencies in the internal control structure design or operation that, in our judgment, could adversely affect DEF's ability to record, process, summarize, and report financial data consistent with management's assertions. These reportable conditions follow:

1. DEF employees do not record hours worked in excess of 8 hours per day.

2. DEF employees sometimes prepare timesheets in pencil.
3. DEF's accounting system does not permit the comparison of budgets with actual expenditures.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to termination costs being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control structure would not necessarily disclose all reportable conditions and, accordingly, would not necessarily disclose all reportable conditions also considered to be material weaknesses as defined above. We conclude that the first two conditions described above are material weaknesses.

RECOMMENDATIONS

We recommend that, for future contracts or subcontracts, DOE require DEF to:

1. Require employees to record and account for all hours worked.
2. Require employees to prepare timesheets in ink.
3. Revise its accounting system to permit a comparison of expenditures with budgeted amounts.

SUBCONTRACTOR'S COMMENTS

The president's comments are included in the notes to exhibit A.

JOHN DOE & COMPANY

By: _____

ACCEPTED BY:

INSPECTOR GENERAL & PAGEE

OFFICE OF

REPORT NUMBER:

Exhibit A
Page 1 of 7DEF Corporation
City, StateClaimed Costs and Audit Results
Termination Settlement Proposal
Subcontract No. Q-1234-5678-T with
ABC, Inc. Under
Contract No. DE-YZ-987654321

	<u>Subcontractor's Claimed Costs</u>	<u>Questioned Costs</u>	<u>Unresolved Costs</u>	<u>Notes</u>
Severance Benefits	\$11,324	\$ 6,432		1
Moving	2,422			
Direct Labor	6,822	39	\$3,955	2
Other Costs	4,187	1,687	2,134	3
General and Administrative (G&A)	3,649	1,109	1,131	4
Additional Settlement Costs	<u>29,059</u>	<u>29,059</u>	<u> </u>	5
Total	<u>\$57,463</u>	<u>\$38,326</u>	<u>\$7,220</u>	

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NOTES TO EXHIBIT AExhibit A
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1. We calculated questioned severance benefit costs of \$6,432 as follows:

	<u>Claimed Costs</u>	<u>Questioned Costs</u>	<u>Reference</u>
Salary	\$ 5,300	\$ 408	a
Fringe benefits	1,790	1,790	b
Overhead	127	127	c
Fringe benefits on accrued vacation	<u>4,107</u>	<u>4,107</u>	d
Total	<u>\$11,324</u>	<u>\$6,432</u>	

- a. DEF paid one month's salary (\$5,300) to an employee who was terminated. DEF representatives stated that ABC's severance pay policy had been adopted in determining the amount of this payment. ABC's policy, however, provides for 4 weeks of severance pay. The monthly salary actually paid to the DEF employee exceeded 4 weeks of pay by \$408. We questioned this amount in accordance with FAR 31.205-6(m), Compensation for Personal Services.
- b. DEF claimed fringe benefits at 33.78 percent of salary costs. The severance pay, however, was not included in the labor base for DEF's 1988 fringe benefit rate computation. In addition, most of the fringe benefits were not allocable to severance pay. We questioned fringe benefits of \$1,790.
- c. DEF claimed overhead costs of \$127 on severance pay. Severance pay was not included in the direct labor base for DEF's overhead rate computation nor do overhead costs benefit severance pay. We questioned overhead costs of \$127 as unallowable in accordance with FAR 31.201-4, Determining Allocability.
- d. DEF claimed fringe benefits at 33.78 percent of DEF's accrued vacation liability of \$12,158 at the subcontract termination date. Fringe benefits were not allocable to this liability for the following reasons.
 - o Vacation costs were expensed as fringe benefits in prior periods and were not included in the labor base for DEF's 1988 fringe benefit rate computation.
 - o Most of the accrued liability (\$9,630) was the president's vacation, and he did not receive this vacation pay at the time of termination. Thus, no fringe benefits on this accrued vacation would be allocable as termination costs.

Accordingly, we questioned \$4,107.

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2. We calculated questioned and unresolved direct labor costs as follows:

	<u>Claimed Costs</u>	<u>Questioned Costs</u>	<u>Unresolved Costs</u>	<u>Reference</u>
Direct labor	\$5,010		\$2,505	a
Fringe benefits	1,692	\$34	1,354	b
Overhead	<u>120</u>	<u>5</u>	<u>96</u>	c
Total	<u>\$6,822</u>	<u>\$39</u>	<u>\$3,955</u>	

- a. DEF proposed direct labor costs of \$5,010 for 120 hours of the president's time. Through November 1988 when DEF submitted its settlement proposal, the president charged 60 hours to the termination. Because of uncertainties regarding the number of additional hours necessary to complete the termination settlement, we classified the difference between the \$2,505 cost of this labor and costs claimed of \$5,010 as unresolved.
- b. DEF claimed fringe benefits at 33.78 percent of direct labor costs. DEF incurred \$1,002 of termination labor costs in FY 1988. The DCAA-approved FY 1988 fringe benefit rate is 30.33 percent. We calculated questioned fringe benefit costs allocable to FY 1988 direct labor as follows:

Fringe benefits claimed on FY 1988 direct labor costs (33.78 percent x \$1,002)	\$338
Fringe benefits applicable to FY 1988 direct labor costs at the 30.33-percent approved rate (30.33 percent x \$1,002)	<u>304</u>
Total	<u>\$ 34</u>

The FY 1989 fringe benefit rate has not been audited. In addition, as explained in Note a, above, we cannot reasonably estimate the remaining termination direct labor costs. Accordingly, we classified fringe benefits of \$1,354 as unresolved (\$1,692 - \$338).

- c. DEF claimed overhead at 2.39 percent of direct labor costs. As explained in Note 2.b, above, DEF incurred \$1,002 of termination labor costs in FY 1988. The DCAA-approved FY 1988 overhead rate is 1.9 percent. We calculated questioned overhead costs allocable to FY 1988 direct labor costs as follows:

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Overhead claimed on FY 1988 direct labor costs (2.39 percent x \$1,002)	\$24
Overhead allocable to FY 1988 direct labor costs at the 1.9-percent approved rate (1.9 percent x \$1,002)]	<u>19</u>
Total	<u>\$ 5</u>

The FY 1989 overhead rate has not been audited. In addition, as explained in Note a, above, we cannot reasonably estimate the remaining termination direct labor costs. Accordingly, we classified overhead costs of \$96 as unresolved (\$120 - \$24).

3. We calculated questioned and unresolved other costs as follows:

	<u>Claimed Costs</u>	<u>Questioned Costs</u>	<u>Unresolved Costs</u>	<u>Reference</u>
Accounting	\$1,980	\$1,030	\$ 800	a
Legal	425		288	b
Clerical	600	221	300	c
Travel	<u>1,182</u>	<u>436</u>	<u>746</u>	c
Total	<u>\$4,187</u>	<u>\$1,687</u>	<u>\$2,134</u>	

- a. DEF proposed 60 hours of accounting services for \$1,980. Through the end of May 1989, DEF's books reflected \$1,920 of accounting fees incurred on termination. However, of these fees:
- o \$1,000 was claimed for the services of a public accounting firm from May through August 1988. The firm's invoices for this period support only \$100 of termination costs. DEF's independent accountant informed us that the claimed costs were based on her timesheets. She could not, however, find the timesheets to support these costs.
 - o \$50 was claimed for the services of a Government contracting consultant hired by DEF to review its termination proposal in FY 1988.
 - o \$570 was claimed for the services of the same consultant in preparing for the DOE audit. We consider costs relating to the audit to be a normal cost of business and not allowable termination costs, as defined by FAR 31.205-42(g), Termination Costs.

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- o \$300 was claimed for 7-1/2 hours spent by DEF's independent accountant in May 1989. Her timesheets for this period (May 12 through 15) indicate that the hours were incurred on "rate calc-TC." DEF's FY 1988 indirect cost rate calculation is dated May 15, 1989. We consider costs of indirect cost rate preparation to be normal costs of business and not allowable termination costs as defined by FAR 31.20542(g).

Based on the above, we consider \$150 (\$100 for public accounting services supported by invoices and \$50 for termination proposal review) supported as incurred termination costs. DEF estimated that accounting costs to complete termination settlement would be \$800 at \$40 per hour). We calculated questioned accounting fees of \$1,030 as follows:

Accounting fees proposed	\$1,980
Less: Supported accounting costs incurred through May 1989	150
Less: Estimated accounting fees through settlement	<u>800</u>
Total	<u>\$1,030</u>

Because of uncertainties regarding accounting fees to complete termination settlement, we classified estimated fees of \$800 as unresolved. DEF's president stated that accounting fees were incurred, but DEF cannot produce documentation.

- b. DEF proposed legal fees of \$425, based on 5 hours at an \$85 hourly rate. DEF's records support \$137 of legal fees incurred in March and May 1988 at a \$75 hourly rate. DEF estimates that 10 additional hours of legal counsel's time will be necessary to review final closing documents. We classified legal fees of \$288 (\$425 claimed less \$137 supported) as unresolved.
- c. DEF proposed clerical costs of \$600 for 40 hours at a \$15 hourly rate. DEF's records support \$79 of clerical costs incurred in typing the settlement proposal. DEF estimates that 20 additional hours of clerical assistance will be necessary at a cost of \$300. We calculated questioned costs as follows:

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Clerical fees proposed	\$600
Less: Clerical costs incurred	79
Less: Estimated clerical costs through settlement	<u>300</u>
Total	<u>\$221</u>

We classified estimated clerical costs of \$300 as unresolved.

- d. DEF proposed costs for a 3-day trip to Atlanta, Georgia, for settlement, as follows:

	<u>Claimed Costs</u>	<u>Questioned Costs</u>	<u>Reference</u>
Air travel	\$ 978	\$438	(1)
Hotel	138		
Per diem	<u>66</u>	<u><2></u>	(2)
Total	<u>\$1,182</u>	<u>\$436</u>	

- (1) We obtained a travel agency quotation for the current, lowest, unrestricted round trip coach fare from Philadelphia, Pennsylvania, to Atlanta, Georgia. We questioned the \$438 difference between proposed airfare of \$978 and the travel agency's quotation of \$540.
- (2) The current Federal Travel Regulations (FTR) meals and incidental expenses rate for Atlanta is \$34 per day--\$1 more per day than proposed. Accordingly, we questioned \$(2) of per diem costs.

We classified remaining travel costs of \$746 as unresolved, because of uncertainties regarding the necessity of the proposed trip.

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4. DEF proposed G&A costs of 14.74 percent of total costs excluding G&A. The DCAA recommended FY 1988 rate is 18.4 percent. The subcontract, however, establishes a ceiling G&A rate of 17.93 percent. In addition, FAR 31.20542(g)(iii) limits indirect costs related to salary and wages incurred as settlement expenses as "payroll taxes, fringe benefits, occupancy costs, and immediate supervision costs." Using this criteria, we calculated an allowable G&A rate to apply to FY 1988 settlement wages of 1.46 percent.

We calculated questioned G&A cost as follows:

G&A costs applicable to questioned non-G&A costs (14.74 x \$8,158)	\$1,202
Difference between claimed 14.74-percent G&A rate and the 1.46-percent rate per audit applied to FY 1988 direct labor (including fringe benefits and overhead per audit (13.28 percent x \$1,325)	176
Difference between claimed 14.74-percent G&A rate and the 17.93-percent ceiling rate applied to FY 1988 nondirect labor costs [(3.19) percent x \$8,435]	<269>
Total	<u>\$1,109</u>

We classified G&A costs allocable to unresolved non-G&A costs of \$6,089 and FY 1989 non-G&A costs of \$1,582 as unresolved [14.74 percent x (\$6,089 + \$1,582) = \$1,131 unresolved].

5. DEF amended its termination settlement proposal on June 3, 1989, to reflect additional costs of \$29,059 associated with the DOE audit. The subcontract includes an audit clause (Clause 7 to Appendix A) giving DOE the right of examination. The costs of audit support are normal costs of doing business. FAR 31.205-42(g) states that allowable settlement expenses are costs "reasonably necessary for--(A) The preparation and presentation, including supporting data, of settlement claims..." Additional costs for audit support do not appear allowable as termination costs.

EXAMPLE OF EQUITABLE ADJUSTMENT PROPOSAL AUDIT REPORT

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITSAUDIT OF
EQUITABLE ADJUSTMENT PROPOSAL
UNDER CONTRACT NO. DE-AC12-345678912
KLM
CITY, STATE

REPORT NUMBER:

PURPOSE AND SCOPE

In response to a request from the U.S. Department of Energy (DOE), Western Area Power Administration (WAPA), we audited costs claimed by KLM as an equitable adjustment proposal under Contract No. DE-AC12-345678912. The \$18,550,000 fixed-price contract was awarded on August 1, 1984, and provided for KLM to design, construct, install, and test the Billings Converter Station in Billings, Montana. On February 19, 1987, WAPA instructed KLM to stop work while WAPA investigated a systems disturbance. KLM was directed to restart work on June 23, 1987 (124 days later). Because KLM was able to conduct some testing during this period, its claim is based on a net delay time of 83 days. KLM's claim also includes costs of 7 days' delay incurred between June 23, 1987, and September 17, 1987, which resulted from trips of relays installed by WAPA. The equitable adjustment proposal totals \$885,538.

The equitable adjustment proposal is the responsibility of the contractor. Our responsibility is to reach a conclusion on the termination settlement proposal based on our audit.

The purpose of our audit was to determine the allowability, allocability, and reasonableness of KLM's costs claimed to use as a basis for negotiating a modification to the contract price.

The audit scope was limited to evaluating historical data and other supporting documentation on which the costs claimed were based and did not include an evaluation of KLM's total internal control system or the technical aspects of the proposal.

As defined in the above scope paragraph(s) we conducted our audit in accordance with generally accepted Government auditing standards that applied to this financial related audit. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the data and records reviewed are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records reviewed. An audit also includes assessing the accounting principles used and significant estimates made by the contractor, as well as evaluating the overall presentation. We used the terms and

conditions of the contract and applicable sections of the Federal Acquisition Regulations (FAR) and the DOE Acquisition Regulations (DEAR) as criteria in evaluating claimed costs. We believe that our audit provides a reasonable basis for our audit conclusions.

We completed our onsite work on September 15, 1988.

CIRCUMSTANCES AFFECTING THE AUDIT

We did not perform a technical evaluation of the equitable adjustment proposal. Accordingly, audit results are qualified pending the outcome of such a review.

KLM's claim is based on an unverifiable estimate that 83 of the 124 days delayed resulted in additional costs. Evidence indicates that other work was being done during the delay period. For example, an electrical subcontractor's invoices indicate that its employees consistently worked overtime during the delay period. Neither KLM project managers nor the electrical subcontractor's personnel maintained time records showing time spent on the original project effort versus time spent because of the delay. Because of this lack of verifiable support for the allocability of costs solely to the delay, we questioned a significant portion of the claim. The notes to exhibit A disclose additional reasons that costs were questioned.

AUDIT RESULTS

Except for the effects, if any, on costs claimed of the matters described in the Circumstances Affecting the Audit section of this report, we questioned \$742,800.

We conclude that, because of the effects of the matters referred to in the preceding paragraph and described in the notes to exhibit A, the equitable adjustment proposal does not represent allowable costs incurred.

Compliance with applicable laws and regulations related to the contract is the responsibility of KLM. As part of our evaluation, we performed tests of compliance with certain provisions of laws and regulations related to the contract. Our objective was not, however, to reach a conclusion on overall compliance with such provisions.

Except for the matters described in the notes to exhibit A, the results of our tests indicate that, for the items tested, KLM complied in all material respects with the provisions of applicable laws and regulations related to the contract. For the items not tested, nothing came to our attention that caused us to believe that KLM had not complied, in all material respects, with those provisions.

We discussed the audit results with the manager of administration, power systems, on September 15, 1988. Also, this report confirms the audit results provided by telephone to WAPA on September 21, 1988.

OTHER MATTERS TO BE REPORTED

In planning and performing our audit of KLM's equitable adjustment proposal, we considered its internal control structure to determine our %PAGEE auditing procedures for the purpose of reaching a conclusion on the proposal and not to provide assurance on the internal control structure.

KLM's management is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit preparation of the financial statement in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purposes of this report, we classified the significant internal control structure policies and procedures as those that relate to the recording and reporting of costs under Government contracts and to ensuring compliance with laws and regulations that have a material impact on costs claimed. These are control procedures designed to ensure that:

- o The breakdown of costs within the accounting system was adequate for cost determination purposes.
- o Specific cost elements were afforded consistent treatment regarding Government and non-Government cost objectives.
- o Allowable and unallowable costs were routinely identified and segregated in the accounting system.
- o Adequate source documentation supported all costs.
- o Assets were safeguarded against loss or unauthorized use or disposition.
- o All accounting data were accurate, reliable, and traceable to underlying source documentation.
- o Contract terms and conditions were known by appropriate personnel and the effects of contract terms and conditions were properly reflected in the accounting records.

For the internal control categories listed above, we obtained an understanding of the design of relevant policies and procedures, determined if they had been placed in operation, and assessed control risk.

We noted certain matters involving the internal control structure and its operation that we consider reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions are matters coming to our attention relating to significant deficiencies in the internal control structure design or operation that, in our judgment, could adversely affect KLM's ability to record, process, summarize, and report financial data consistent with management's assertions. These reportable conditions follow:

1. Employees prepare timesheets in pencil and do not authorize changes. Consequently, unauthorized timesheet changes could be made and go undetected.
2. Employees do not prepare travel expense vouchers. Employees charge travel expenses directly to company credit cards, and the bookkeeper records charges to benefiting activities by matching monthly invoices to submitted receipts. The failure to prepare complete travel records could result in misallocation of travel expenses.
3. KLM does not have written accounting procedures.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the costs claimed being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control structure would not necessarily disclose all reportable conditions and, accordingly, would not necessarily disclose all reportable conditions also considered to be material weaknesses as defined above. We conclude that the first two conditions described above are material weaknesses.

RECOMMENDATIONS

We recommend that DOE instruct KLM to:

1. Require employees to prepare timesheets in ink and authorize all timesheet changes.
2. Require employees to prepare travel vouchers; these vouchers should be authorized by management.
3. Document its accounting procedures.

CONTRACTOR'S COMMENTS

KLM did not comment on the audit results.

JOHN DOE & COMPANY

By: _____

ACCEPTED BY:

INSPECTOR GENERAL

OFFICE OF

REPORT NUMBER:

Exhibit A
Page 1 of 4KLM
City, StateClaimed Costs and Audit Results
Equitable Adjustment Proposal
Under Contract No. DE-AC12-345678912

	<u>Amount Claimed</u>	<u>Audit Results Questioned Costs</u>	<u>Notes</u>
Direct Labor (On Site in Delay Status)	\$346,608	\$346,608	1
General Administrative	377,094	275,296	2
Per Diem	51,875	51,875	3
Equipment Rental	42,968	42,968	4
Direct Labor (Delays Caused by Relay Trips)	33,981	26,053	5
Credit for Staged Fault Tests	<u><10,000></u>	<u> </u>	6
Total Costs	\$842,526	\$742,800	
Profit	<u>43,012</u>		7
Total Costs Plus Profit	<u>\$885,538</u>		

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NOTES TO EXHIBIT AExhibit A
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1. We questioned all direct labor costs (on site in delay status) for the following reasons:
 - a. KLM claimed labor costs of \$278,050 for five commissioning engineers and a commissioning assistant. The costs were computed using average intercompany billing rates of \$610 per day for each commissioning engineer and \$300 per day for the commissioning assistant. KLM representatives could not provide documentation supporting the accuracy of these rates. Additionally, KLM employees did not maintain records of actual time allocable to the delay versus time spent on other work.
 - b. KLM claimed labor costs of \$68,558 for an electrical subcontractor. The claimed costs were a portion of the subcontractor's costs during the delay period, and the subcontract invoices do not distinguish between electrician time allocable to the delay and time spent on other work.
2. We questioned general administrative costs are as follows:
 - a. Project management costs included labor costs of \$107,716 for an assistant program manager and a project administrator. KLM computed these costs based on intercompany billing rates of 146 German marks (approximately \$81) per hour for each employee, but could not provide documentation to support these rates. Additionally, these two employees did not maintain records of actual time allocable to the delay versus time spent on other work.
 - b. Project management costs included \$23,013 for salary, fringe benefits, and "office" costs of a program manager and onehalf of a secretary in Alabama, and \$19,916 for the salary, fringe benefits, automobile, and per diem of a site superintendent. The program manager's title is "marketing manager H.V.T.S.," and none of these employees maintained records of actual time allocable to the delay versus time spent on other work. (We also noted that KLM estimated fringe benefits at 31 percent; its records supported a 26-percent fringe benefit rate, resulting in a \$731 difference.)
 - c. KLM claimed costs of home leave incurred by German-resident employees working in Montana. It is KLM's policy to allow employees one trip home after every 9 months of service abroad. The 4-month delay resulted in additional trips home for the German-resident employees. KLM's claim, however, included the cost of two trips home for two KLM employees. We questioned the leave costs of \$3,641 for the second trips.

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- d. KLM's calculations of travel, site transportation, telephone, and office supplies exceeded its claim by \$13,095. These calculations, however, were based on unverifiable estimates of the allocability of these costs to the delay. For example, claimed travel costs included the cost of trips taken by the program manager and project administrator from March through December 1987. Accordingly, we questioned the \$45,610 included in the claim.
 - e. KLM claimed \$8,430 for interest lost on delayed milestone payments. These costs are unallowable in accordance with FPR 1-15.205-17, Interest and Other Financial Costs.
 - f. KLM claimed cost increases of \$11,000 for the contract's maintenance period. The cost increases were computed based on 11 months, which is apparently the difference between the maintenance start date from the original contract and the actual start date. KLM representatives explained that the cost increases claimed were the result of losses in currency exchange rates and increases in commissioning engineers' rates. KLM could not provide documentation to support this claim. We questioned \$7,000 (for 7 months) of the cost increase as unallocable to the delay. We questioned the remaining \$4,000, because it is unsupported.
 - g. KLM claimed overhead costs at 10 percent of direct labor costs, purchased services costs, and travel costs. KLM performed a calculation indicating that actual overhead rates were 36.3 percent of labor costs and 2.8 percent of purchased services and travel costs. KLM did not, however, provide documentation to support this calculation of overhead costs. Accordingly, we questioned overhead costs claimed of \$54,625.
 - h. KLM claimed insurance costs allocable to the delay using a 360-day year in its calculation. We recomputed the cost based on an actual 365-day year and determined that \$1,345 of insurance costs was overclaimed.
3. KLM claimed per diem costs included allowances for U.S. tax reimbursements. It is KLM's policy to pay all U.S. tax liabilities incurred by German employees. This allowance includes Federal income taxes unallowable in accordance with FPR 1-15.205-41, Taxes. Because KLM could not identify or segregate Federal income taxes, we questioned the entire tax allowance of \$14,820. Also, we questioned the \$37,055 balance of claimed per-diem costs, because KLM did not maintain records supporting the allocability of time to the delay versus time spent on other work.

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4. KLM claimed equipment rental costs incurred before the February 19, 1987, stop work order and after the June 23, 1987, instructions to restart work. We questioned \$7,028, because it is unallocable to the delay. Also, we questioned the \$35,940 balance of equipment costs, because we could not determine if the costs were allocable only to the delay and that the equipment was not used for other work.
5. We questioned direct labor (delays caused by relay trips) costs as follows:
 - a. Because of an arithmetic error, KLM overclaimed direct labor costs by \$720. We questioned this cost and the associated overhead of \$72.
 - b. As explained in Notes 1 and 2 above, labor rates for commissioning and project management employees are unsupported. Accordingly, we questioned \$21,350.
 - c. As explained in Note 3, per-diem costs claimed included an allowance for U.S. tax reimbursements. Per diem claimed for the 7-day part of the delay included \$1,260 of such allowances.
 - d. As explained in Note 2 above, overhead costs claimed are unsupported. These costs, net of \$72 questioned in Note 5.a, are \$2,651.
6. KLM could not provide documentation to support the \$10,000 credit for staged fault tests. We could not determine if this credit was over or understated.
7. The proposed profit is subject to the contracting officer's review and determination.

CHAPTER 20AUDITING FEDERALLY ASSISTED PROGRAMSA. SCOPE OF CHAPTER

Section V of the Manual, consisting of this chapter and related exhibits, deals with audits of Federally Assisted Programs. This section provides a structured approach to evaluating audits of Federally Assisted Programs performed by non-Federal auditors. It outlines the responsibilities of AO and Regional Offices.

B. BACKGROUND

DOE provides substantial grant funds to State and local governments and other non-Federal domestic organizations. In accepting grant funds, the recipients are responsible for carrying out the programs efficiently, economically and effectively. They assume the responsibility for having the programs audited in accordance with Federal requirements.

In the past, programs were audited on a grant-by-grant basis, with considerable duplication and overlapping of audit authority and performance among State and local auditors and their Federal counterparts. In response, OMB mandated fundamental changes in the scope of and reliance to be placed on audits.

OMB Circular A-128 calls for organization-wide audits of grantee financial operations (see exhibit A, A:AM20EXA.WPF). The audits must include, at a minimum, an examination of the systems of internal controls established to ensure compliance with laws and regulations affecting the expenditure of Federal funds, financial transactions and accounts, and financial statements and reports of recipient organizations.

The performance of audits on an organization-wide basis poses several oversight problems for Federal agencies funding State and local governments and other non-Federal domestic organizations. The recipients frequently receive funds from many sources, carry out a multiplicity of activities, and sometimes act as conduits in channeling funds to subgrantees. In multifunded agencies, DOE programs may be substantial in dollar terms, but insignificant in relation to other programs carried out by recipients. In these cases, DOE programs may receive little or no coverage. Moreover, organization-wide audit reports may not be explicit about the source and application of funds or the extent of audit coverage. This makes it difficult to judge whether adequate financial and compliance tests of DOE grants have been made.

Organization-wide audits also raise questions about how to minimize or prevent overlapping and duplication of audit efforts in circumstances where recipients receive government funds from two or more Federal agencies. OMB Circular A-128 addresses this problem by establishing "cognizant agencies" to assume audit responsibility for designated recipients. If independent audits arranged for by the recipients meet prescribed standards, Federal agencies are to rely on them. If supplemental audit coverage is needed it must build upon

the work already done. For example, OMB also requires Federal agencies to rely on audits made by non-Federal auditors to the maximum extent practicable. OMB Circular A-73 provides that:

Reports prepared by non-Federal auditors will be used in lieu of Federal audits if the reports and supporting workpapers are available for review by the Federal agencies, if testing by Federal agencies indicates the audits are made in accordance with generally accepted auditing standards (including the audit standards issued by the Comptroller General), and if the audits otherwise meet the requirements of the Federal agencies.
(Underscoring supplied.)

Auditors involved in audits of Federally Assisted Programs are responsible for understanding and implementing, where appropriate, policies and procedures discussed in Parts I, II, and III of this Manual.

C. IMPLEMENTATION PLAN

OMB originally gave the DOE IG audit cognizance over 36 State and local organizations, but due to subsequent reorganizations and other changes, the actual number was 5 as of October 1, 1990. The Single Audit Act of 1984 (Public Law 98-502(7)(b)) requires that a cognizant agency:

- o ensure that annual or biennial audits are made in a timely manner and in accordance with audit requirements;
- o ensure that audit reports and corrective action plans are sent to appropriate Federal officials;
- o coordinate, to the extent practicable, audits done by or under contract with other Federal agencies; and
- o ensure that additional audits build upon the audits that have been performed.

The list provided in exhibit B (A:AM20EXB.WPF) shows the assignment of audit cognizance for State and local agencies for which the DOE is currently responsible. Regional responsibilities include monitoring and controlling audits of Federally Assisted Programs performed by nonFederal auditors. AO is responsible for ensuring compliance with OIG's audit responsibilities for grant programs; supporting and assisting OIG regional offices; and tracking audit findings and questioned costs into DOE's DARTS.

D. REPORTING

Grant audits can take a variety of forms, depending on the precise audit objective. They may include audits of costs incurred, program results, economy and efficiency, and others. Therefore, no standard report format is prescribed. Instead, auditors should refer to the reporting sections of this Manual which are most relevant to the audit objective.

E. AO'S GRANT AUDIT RESPONSIBILITIES

This section describes AO's role in ensuring compliance with the OIG's audit responsibilities for grant programs; supporting and assisting the %PAGEE Regional Offices; and tracking audit findings and questioned costs into DOE's audit report tracking system.

1. Oversight Over DOE-Assisted Grants. By delegation of authority from the AIGA, AO is responsible within DOE for ensuring compliance with the provisions of OMB Circular A-128. In carrying out its responsibilities, AO is guided by the following principles:

a. OMB Circular A-128 - Compliance with OMB Circular A-128 is a mandatory element of the OIG's responsibilities and must be discharged effectively.

b. Organization-Wide Audits - DOE relies on organizationwide audits for assurances that the recipients it supports are handling funds properly and in compliance with laws and regulations.

c. Reliance of Other Federal Agencies - Other Federal agencies whose funds are included within the scope of DOE-cognizant audits rely on OIG oversight for assurance that the audits meet prescribed standards and can be relied upon by their departments.

d. Outreach Program - Programs subject to audit are widely dispersed throughout the country and, while small in some locations, are large in the aggregate. Organization-wide audits by independent accountants are the "first-line of defense" against fraud, waste and abuse in these programs. DOE can play an effective role in upgrading the quality of the audits performed through an effective outreach program.

e. Internal Reporting - Questioned costs, program deficiencies and poor internal controls identified in independent auditors' reports may be symptomatic of more serious problems which need to be examined by OIG in a geographical or functional basis. There must be an internal reporting mechanism for bringing problems or deficiencies to the attention of OIG headquarters to be able to assess them from a Departmental perspective.

f. Prompt Action - The value of auditing is diminished unless prompt and effective action is taken on the independent auditors' findings.

g. AO Methodology - AO will discharge its responsibilities by (1) providing general guidance and assistance to the Regional Offices; (2) helping resolve problems or issues that cannot be dealt with effectively at the Regional Office level; and (3) monitoring the process for resolving findings.

2. Guidance and Assistance to Regional Offices. AO will provide information to the Regional Offices to help establish planning priorities and resolve issues that cannot be handled effectively at the local level.

a. Planning - DOE-funded grant assistance programs are widely dispersed geographically. They amount to substantial dollar amounts overall. While many audits are made, it is difficult to judge whether the bulk of the

program dollars spent receive appropriate audit coverage for a variety of reasons:

- o Some recipients funnel most of their DOE funds to subgrantees, but the audit report does not comment on the audit coverage at the subgrantee level.
- o Some audit reports lack specificity about the source and application of funds and the extent of audit coverage.
- o DOE's programs may be so small relative to other Federal assistance to the audited entity that they are excluded from the scope of the audit (i.e., they do not meet the audit "threshold").
- o There is no assurance that all audit reports are received on DOE-funded assistance, particularly where DOE is not cognizant.

AO will provide the Regional Offices with information on grants, by recipient and location. The Regional Offices should use this information to rank the recipients by program, size, or other criteria that will provide for balanced audit coverage. Special attention should be given to audits involving recipients in the upper quarter. Reports on their programs should be evaluated carefully and quality reviews undertaken if the results are inconclusive or questionable.

b. Issue Resolution - Regional Offices occasionally may encounter issues which cannot be resolved at the local level. These matters should be brought to AO's attention. Examples include (1) intergovernmental or interagency problems with the timing or scope of audits; (2) staffing limitations; and (3) the need for a Quality Control Review (QCR).

AO will work cooperatively with the Regional Offices in deciding on an appropriate course of action.

3. Tracking Audit Exceptions. AO will review quarterly exception reports submitted by the Regional Offices to identify questioned costs or significant deficiencies. AO will also compile overall data on audit findings and accomplishments for inclusion in the IG's semiannual report.

F. REGIONAL OFFICES' GRANT AUDIT RESPONSIBILITIES

This section outlines Regional Office procedures to be followed in fulfilling their delegated oversight responsibilities.

1. Delegated Oversight Responsibilities. Regional Offices play a significant role in discharging the OIG's responsibilities for monitoring and controlling audits of Federally Assisted Programs performed by non-Federal auditors.

Under the OIG's decentralized operations, day-to-day contacts with the non-Federal auditors, and reviews of their audit reports, are made by Regional Office staff. They provide technical advice and assistance; establish liaison with other Federal audit agencies; perform desk reviews of audit reports; arrange for Quality Control Reviews of audit organizations and their work;

recommend procedures to address deficiencies; and perform other functions needed to help the OIG effectively discharge its responsibilities.

Regional Offices will submit the following periodic reports on their activities to AO.

"As-Needed" Reports

- o Report on Potential Fraud or Abuse Situations
- o Report on Substandard Audits

Quarterly Reports

- o Audit Status Report
- o Quarterly Exception Report

These reports will identify backlogs, processing delays in initiating or completing audits, significant audit findings, and problems or issues the AIGA should be aware of. The reports are an opportunity to bring important problems and accomplishments to the attention of the Headquarters staff and obtain advice or assistance where needed.

2. Assistance to Audit Organizations. Regional Offices are responsible for formally establishing audit liaison arrangements with the recipient organizations for which they have been assigned audit cognizance. The reasons for establishing and maintaining contacts are

- o to help ensure that high quality audit reports are produced by auditors engaged by recipient organizations;
- o to ensure that grantees and their auditors understand what is expected of them by communicating and emphasizing OMB requirements, General Accounting Office Standards and Guidelines, and AICPA Pronouncements;
- o to promote timely performance of audit work; and
- o to encourage a mutual interchange of views on technical problems or issues, auditing techniques, staff qualifications, etc.

Regional Offices also need to establish appropriate contacts with other Federal audit groups whose agencies fund programs included in organization-wide audits for which DOE has audit cognizance. Within the limit of available resources, the Regional Offices are encouraged to participate in related training programs sponsored by professional organizations.

3. Desk Reviews of Audit Reports. Regional Offices are responsible for reviewing all audit reports submitted for cognizant audit agency processing. The initial process, referred to as a desk review, will judge whether the audit reports meet prescribed standards and can be relied upon in lieu of an OIG audit. Regional Offices should complete the desk review within 60 days after receipt of the audit report.

Matters to be addressed in the course of desk reviews include an evaluation of the qualifications and independence of the auditors; assessment of the professionalism with which financial statements have been compiled, certified and qualified; references in the report to positive or negative assurances that compliance requirements have been reviewed; and comments on internal control procedures and weaknesses.

Regional Offices also are responsible for reviewing audit reports submitted by other cognizant Federal audit agencies to determine whether the audits satisfy DOE's auditing needs.

4. Quality Control Reviews. As discussed in paragraph 2, Regional Offices are responsible for ensuring that audits of Federally Assisted Programs meet acceptable quality and compliance standards.

If the Regional Office decides, based on its desk review, that there is a reasonable basis for questioning the work performed by non-Federal auditors, a review of working papers and/or independent field tests should be scheduled for performance at the earliest practicable time. Transmittal of the audit report should not be held up pending completion of the additional work. Instead, the report should be sent to action parties with a memorandum explaining why the additional work is needed and its expected completion date.

If there are questions about the work performed on noncognizant audits, the Regional Offices should obtain clarification from the cognizant Federal audit agency, and if necessary, arrange for supplemental audit coverage.

5. Peer Reviews. Audit organizations conducting government audits should have an appropriate internal quality control system in place and participate in an peer review at least once every 3 years by an organization not affiliated with the organization being reviewed. Peer reviews, such as those conducted through or by the AICPA, National State Auditors Association, Intergovernmental Audit Forums, GAO, and the Institute of Internal Auditors, would be acceptable.

Peer reviews are comprehensive reviews of non-Federal audit organizations and their work and are made to determine that

- o the organization's internal quality control system is in place and operating effectively, and
- o auditing standards are being followed in its audit work, including its government audits.

Regional Offices should evaluate the results of desk reviews and any prior QCR's that have been performed or are scheduled. If a peer review was performed, obtain a copy of the results from the Federal audit organization or nonFederal auditor. If a review is scheduled, obtain the name of the responsible audit organization, the date the assessment will begin, and the estimated completion date.

In transmitting an audit report where reliance has been placed on a peer review made by another Federal audit organization, the addressee should be

told which federal audit organization performed the peer review and the scope of its review.

6. Distribution of Audit Reports and Findings. After each audit report is reviewed by the Regional Office, it should be distributed to Federal audit offices responsible for the programs included in the audit scope. The report should be accompanied by a transmittal letter or memorandum highlighting problems or deficiencies requiring action.

The Regional Office has special responsibilities for handling cross-cutting issues (i.e., findings that affect other Governmental agencies and cannot adequately be resolved through independent action by DOE). In these cases, the Regional Office must enter into a coordinating arrangement with OIGs of the other agencies to affix responsibilities for overseeing resolution of the findings.

7. Processing Notifications of Irregularities; Fraud and Abuse. Regional Offices are responsible for promptly informing AO if irregularities in DOE programs come to their attention through reviews of audit reports or other avenues. If irregularities affect another Government agency, the Regional Office should immediately inform the affected agency's auditors of the nature of the irregularities and a recommended course of action. The term irregularities refers to matters such as intentional distortions of financial statements; misappropriation of assets; falsification or alteration of data; use of false or misleading records or documents; collusion; and conflicts of interest. Regional Offices should be particularly alert to situations involving fraud or abuse. These situations must be reported to AO without delay.

8. Referrals of Major Inadequacies or Substandard Work. Regional Offices are responsible for referring instances of inadequate or substandard audit work to appropriate professional and/or regulatory bodies. Referrals should be made if inadequacies make the report so persuasively inadequate that users cannot rely on it; or if substandard work is of such a serious nature that it warrants correction by the auditor.

9. Workload Control. Regional Offices are responsible for maintaining a workload register to keep track of audits scheduled by and received from non-Federal auditors. Permanent files should be maintained on each organization for which DOE has audit cognizance. The files should include background information about the organization, prior audits, compliance with accounting standards, and known problems or weaknesses. A record of all DOE-related audits made by the non-Federal auditors should be included, together with the results of all OIG reviews.

10. Workload Planning and Scheduling. Regional Offices should provide sufficient time and resources in their audit plans to permit them to carry out their responsibilities for ensuring compliance with OMB Circular A-128. Staffing resources must be sufficient to allow for technical assistance, timely processing of audit reports, and field verifications where the audit work performed is considered questionable. Plans should emphasize coverage of programs that have received relatively substantial DOE assistance.

11. Cooperative Audit Arrangements. In some instances, Regional Offices may request other Federal audit agencies to participate in an organization-wide audit of a particular State or local governmental unit. Alternatively, other Federal agencies may request Regional Office assistance. These arrangements may be consummated by the Regional Offices if they contribute to DOE's auditing objectives.

12. Internal Management Reports. Regional Offices are responsible for providing the periodic reports to AO that are discussed in sections F.1. and 7.

G. GRANT AUDIT GUIDES AND PROCEDURES FOR REGIONAL OFFICES

This section elaborates on Regional Office responsibilities for monitoring State and local government compliance with public laws and OMB circulars related to audits of Federally Assisted Programs.

1. Outreach Activities. OMB Circular A-128 requires the cognizant audit agency to provide technical advice and liaison to State and local governments, independent auditors and recipient organizations. A clear understanding of OMB requirements by the recipient organization and its auditor(s) contributes to organization-wide audits and reports of a higher quality than otherwise might be obtained. The best way to provide this assistance is "up front" before audit work begins. By discussing audit requirements and planned approaches, the cognizant agency can influence the conduct of the audit and ensure that mandated standards and objectives are incorporated in the audit plan and program. Technical assistance should also be provided on an "as needed" basis thereafter.

a. Control Log for Recipient Single Audit Reports - OMB Circular A-128 requires that each cognizant audit agency establish and maintain a report control log for all state and local government entities to which the agency provides Federal financial assistance. Control logs should be maintained for each assigned recipient organization to record the items shown in exhibit C (A:AM20EXC.WPF) for cognizant organizations and exhibit D (A:AM20EXD.WPF) for noncognizant organizations.

The control log should be consistently maintained throughout the audit organization. As actions are taken with respect to each report, they should be recorded on the control register. Individual recipient files should be maintained to facilitate easy retrieval of single audit reports and all documentation pertaining to their processing.

b. Effecting Timely Performance of Audit Work - OMB Circular A-128 requires each State and local government that receives a total amount of Federal financial assistance exceeding a specified threshold to have an audit made annually. In some circumstances, the audit can be made biennially. Regional Offices are responsible for taking requisite steps to enforce compliance with this requirement.

The Regional Office should contact each recipient organization for which it has cognizance approximately six months before the established due date for

submission of the audit report. This contact may be verbal or in writing, but it should be documented. At a minimum, the contact should produce knowledge of

- o the independent auditor that has been engaged;
- o when the audit is scheduled to begin; and
- o the expected date for submission of the audit report.

If the audit report is not received by the Regional Office on or before the expected due date, the Regional Office should determine why the report was delayed and obtain a revised submission date.

If the time slippage is significant, or the recipient has not properly exercised its responsibility to obtain timely and effective audits, the Regional Office should promptly

- o discuss the matter with the top recipient officials;
- o remind them of legal and administrative requirements;
- o elicit a response on their plans to comply with audit requirements; and
- o refer the situation to AO for resolution if the response is not satisfactory. The audit agencies of other Federal organizations whose programs and activities are affected must also be notified.

c. Liaison with Recipient Organizations - Regional Offices should formally establish audit liaison with each cognizant organization. The recipient organization should be informed in writing of its responsibilities to arrange for audits performed in accordance with the requirements of OMB Circular A-128.

OMB Circular A-128 requires that recipients determine whether subrecipients spent Federal assistance funds in accordance with applicable laws and regulations. This requirement should be communicated to recipient organizations and compliance should subsequently be verified through discussions and observations.

The Regional Offices should ensure that recipient organizations have in their possession the reference material they need to properly conduct the audit. Requirements in the Yellow Book dealing with the qualifications of auditors and scope of audit should be communicated.

Recipient organizations should be informed of the need to include in their engagement agreements with auditors the OMB requirements for an organization-wide audit; a compliance review; an internal control evaluation; expressions of opinion; and inclusion of a management corrective action plan in audit reports or management letters. These requirements in many cases go beyond the standard opinions and comments usually presented in audit reports.

Specifically, the auditor should know the requirement to express an opinion on financial statements and to provide comments on

- o financial statements;
- o compliance;
- o internal control;
- o scope of audit;
- o accuracy and completeness of financial reports and claims for advances or reimbursement to Federal agencies; and
- o corrective action taken or planned by the recipient.

"Up front" discussions with the recipient organization and its auditors should also include agreements on

- o who to contact when questions arise;
- o when the audit report will be submitted; and
- o how and to whom the report will be sent.

Liaison with recipient organizations is a continuous and interactive process which should be actively pursued as a way of communicating ideas and suggestions and resolving differences. Assistance may be prompted by requests from recipients and their auditors. Requests should be answered promptly and effectively. Technical assistance should be provided if necessary to communicate changes in audit requirements and policies.

d. Liaison with Other Federal Agencies - It is not necessary for the Regional Offices to be familiar with the programs of other Federal agencies. At a minimum, the Regional Offices should establish appropriate contacts with the other audit groups, particularly the agencies whose programs are usually audited along with DOE programs when organization-wide audits are made.

e. Liaison with Professional Organizations - Regional Offices are encouraged to participate (to the extent resources permit) in training programs sponsored by auditor and recipient professional organizations.

2. Desk Reviews. Where DOE has been assigned audit cognizance, the Regional Offices will review all audit reports prepared by non-Federal auditors, using the review procedures provided in exhibit E (A:AM20EXE.WPF). Regional Offices will also review the reports submitted by other cognizant audit agencies (nongnizant to DOE), using the review procedures provided in exhibit F (A:AM20EXP.WPF).

Unless staff resources prevent it, reports should be subjected to the desk review process within 60 calendar days from receipt. If this requirement cannot be met, AO and the affected Federal agencies should be notified of the reasons. In some cases, it may be necessary to schedule reviews of

working papers or undertake independent verifications of the audit work performed. In these cases, the Regional Office should transmit the audit report accompanied by a letter explaining that the additional verification work is in progress. At a minimum, a desk review should consider the following elements:

a. Qualifications of Auditors - The report should be examined for indications that the auditor does not meet the qualification or independence requirements for auditors. If the report was prepared by a public accountant, and it is not clear that the auditor is a CPA or public accountant licensed on or before December 31, 1970, reviewers should satisfy themselves on this point by checking with State licensing authorities. If the Auditor is a State or local government auditor, the reviewer should ascertain whether the auditor is independent of the entity being reviewed.

b. Financial Statements - The reviewer should judge whether the audit report includes

- o financial statements (including footnotes) of the recipient organization;
- o breakdowns that include all Federal funds known by the Regional Office to have been received by the auditee;
- o comments on the financial statements;
- o identification of the statements examined and the periods covered;
- o identification of the various programs for which the organization received Federal funds, and the amount of the awards;
- o a representation that the audit was done in accordance with GAGAS;
- o an expression of an opinion as to whether the financial statements are fairly presented in accordance with generally accepted accounting principles; and
- o comments on the reasons for any qualifications if an unqualified opinion cannot be expressed.

c. Compliance - The reviewer should ascertain whether comments on compliance

- o appropriately contain an expression of positive assurance with respect to compliance with requirements for tested items, and negative assurance for untested items;
- o indicate which compliance items were tested, the nature of the tests performed, the extent of the tests, and the results;
- o indicate that the operations of the grantee are (or are not) in conformance with compliance requirements that could have a material effect on the financial position of the grantee; and

- o appropriately contain an expression on material instances of noncompliance related to programs financial statements or award, claim, fund, or group of accounts being tested.
- d. Internal Controls - The reviewer should decide whether comments on internal control are appropriately addressed in the audit report.
- e. Other Matters - The reviewer should examine the report to see whether it appropriately comments on
 - o the accuracy and completeness of financial reports and claims for advances or reimbursement to Federal agencies; and
 - o corrective action taken or planned by the recipient.

Where there are material deficiencies in the work performed, as evidenced by errors of omission or commission, or where the reviewer is unable to determine the adequacy of the work performed because of a lack of information, it is incumbent on the Regional Office to schedule additional work to judge the adequacy of the audit and decide on a remedy. The additional work can consist of a workpaper review or independent field test. The techniques to be followed are discretionary as long as the end objective is achieved.

3. Quality Control Reviews. While desk reviews are an effective means for determining whether audit reports meet the requirements of OMB Circular A-128, they do not address the quality of the work supporting the audit report. Where the Regional Office has concerns about the adequacy of the audit work, supplemental reviews and tests should be arranged (see exhibit G, A:AM20EXG.WPF, for an example of a uniform QCR review guide). Workpapers generally should be reviewed within 90 calendar days of receipt of the audit report. At any time that problems or questions arise about a project or audit, a review of the audit workpapers may be made. Where QCRs are not performed due to lack of resources or other reasons, the Regional Office should document this fact and the reasons why.

- a. Workpaper Reviews - The minimum supplemental test is a review of the workpapers supporting the audit report. The review may be
 - o narrowly focused to determine whether a certain portion of the audit work was properly performed; or a
 - o comprehensive a review of the quality of one or more segments of the audit work performed.

The extent of the tests will depend on factors such as

- o the materiality of the dollar amounts involved;
- o the vulnerability of the program to fraud or abuse;
- o the results of prior reviews of the independent auditor's work;
- o prior findings or weaknesses in the program being audited; and

- o the significance of the suspected audit problems that prompted the workpaper review.

b. Field Tests - In some cases, the Regional Office may conclude that a workpaper review is not enough to allow it to reach an informed opinion about the quality of the audit work performed. Where this is so, the Regional Office will arrange for a visit to the audit sites to verify, on a sampling basis, the data used to support the audit report. Field testing is an extension of workpaper reviews and generally should be undertaken within 60 days of receipt of the audit report.

4. Distribution of Audit Reports. After audit reports have received and reviewed, they should be distributed to the Federal audit agencies responsible for the programs included in the scope of audit.

a. Internal Distribution - The Regional Offices should follow established internal procedures in distributing copies of audit reports for action by DOE contracting officers.

b. External Distribution - The audit Report should be distributed to noncognizant agencies with a transmittal letter or memorandum that highlights findings or matters requiring action by the addressee.

c. Special Handling for Crosscutting Issues - When the audit report contains a finding which cannot be adequately resolved through unilateral actions by DOE, the Regional Office's letter or memorandum transmitting the report should identify the crosscutting finding and propose a coordinating arrangement to jointly resolve it. The arrangement should be discussed in advance to ensure acceptance by the action parties.

5. Audit Resolution. When audit reports, prepared in accordance with OMB Circular A-128, contain findings requiring action by DOE officials, the Regional Office will compile information on questioned costs. This information will be sent to AO in Quarterly Exception Reports as described in the following sections.

Within DOE, the responsibility for tracking resolution of audit findings rests with the Office of the Controller, which maintains DARTS. To ensure that matters requiring Departmental resolution on Quarterly Exception Reports are appropriately recorded, Regional Offices will trace information on the Quarterly Exception Reports to the DARTS system. When findings require resolution by one or more other Federal agencies (i.e., crosscutting issues), the Regional Offices should track the resolution action to its satisfactory completion. With respect to findings which do not involve DOE funds or programs, followup action is the responsibility of the affected agency's auditors.

6. Cooperative Audit Arrangements. Where a single audit performed by independent auditors provides Federal agencies with the information and assurances they need to carry out their overall responsibilities, they will rely on the single audit. However, a Federal agency shall make any additional audits as are necessary to carry out its responsibilities under Federal laws and regulations. Any additional audit efforts shall be planned and carried out in a way that will avoid duplication. In some cases, the Regional

Office may find it desirable to perform additional work by entering into arrangements with other Federal audit agencies to jointly conduct these reviews.

The Regional Office may ask for participation of other agencies where DOE is cognizant, may volunteer to participate in reviews where another Federal agency is cognizant, or may be asked to participate. If it is in DOE's interests to do so, the Regional Offices may initiate or agree to such arrangements. If they are entered into, the following general rules apply:

a. Lead Audit Agency - This agency

- o convenes and chairs meetings of participating audit agencies;
- o provides technical advice regarding its own agency's programs and coordinates technical advice received from participating audit agencies;
- o obtains major compliance requirements and transmits them to the auditors;
- o reviews audit plans and incorporates the views of participating cognizant audit agencies;
- o informs other affected audit agencies, whether participating or not, of irregularities uncovered; and
- o assures that the audit report is received, reviewed and distributed.

b. Participating Audit Agency - A participating audit agency

- o participates in the review if desirable to represent the Government's interests;
- o attends meetings convened by the lead cognizant audit agency;
- o provides technical assistance and advice to the lead cognizant audit agency and to the recipient organization and auditors, after coordinating with the lead cognizant audit agency;
- o obtains and provides to the lead cognizant audit agency major compliance requirements in accordance with OMB policy for programs of its agency;
- o advises the lead cognizant audit agency of suggested adjustments in scope for segments of audit pertaining to its agency's programs;
- o advises the lead cognizant audit agency of significant crosscutting audit problems; and
- o oversees supplemental audit work, if any, in areas of its special expertise.

7. Internal Management Reports. To effectively discharge its oversight responsibility, AO must receive timely information on issues, problems, and accomplishments as they relate to audits of DOE-financed grant programs. These data will be used to:

- o provide assistance to Regional Offices in resolving problems that cannot be handled locally;
- o measure accomplishments attributable to the audits;
- o pinpoint systemic problems which may need to be examined by OIG on a geographical or functional basis; and
- o enable the OIG to assess compliance with OMB Circular A-128.

Four types of management reports have been developed. They are:

a. Quarterly Report on Recipient Organizations Not Complying With A-128 Requirements - This report (see exhibit H, A:AM20EXH.WPF) will highlight recipient organizations who have not complied with the requirement for biennial (or annual) audits. It will also disclose the status of processing within the Regional Office. Any problems in obtaining timely audits can be brought to the attention of AO for follow-through at the Headquarters level.

b. Quarterly Exception Reports on Questioned Cost - This report (see exhibit I, A:AM20EXI.WPF) shows costs questioned in relation to total DOE expenditures for the period of audit. If significant amounts are questioned, the findings can be tracked to DOE's audit resolution system. If audits consistently show on questioned costs, this may be an indication of superficial audits or scope limitations.

c. Quarterly Exception Report on Material Compliance And Internal Control Weaknesses - This report (see exhibit J, A:AM20EXJ.WPF) shows material weaknesses in compliance and internal controls. Where these problems exist, the probability of irregularities exists and the agencies should be included in the universe of locations to be reviewed through quality control assessments or independent OIG audits.

d. Report on Potential Fraud Or Abuse Situations - This report (see exhibit K, A:AM20EXK.WPF) should be completed and sent to AO immediately upon learning of actual or potential fraud or abuse. The magnitude of the suspected problem, the nature and circumstances which created the problem, and recommendations of the Regional Office should be outlined in the report.

e. Report of Substandard Audits - This report (see exhibit L, A:AM20EXL.WPF) discloses inadequacies in audits of Federally assisted programs performed by independent auditors. Where deficient audit work has been identified, OIG has a responsibility for bringing the matter to the attention of AO and accreditation agencies and seeking remedial action.

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503
(ON OMB LETTER HEAD)

April 12, 1985

CIRCULAR No. A-128

TO THE HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: Audits of State and Local Governments.

1. Purpose. This Circular is issued pursuant to the Single Audit Act of 1984, P.L. 98-502. It establishes audit requirements for State and local governments that receive Federal aid, and defines Federal responsibilities for implementing and monitoring those requirements.

2. Supersession. The Circular supersedes Attachment P, Audit Requirements, of Circular A-102, "Uniform requirements for grants to State and local governments."

3. Background. The Single Audit Act builds upon earlier efforts to improve audits of Federal aid programs. The Act requires State or local governments that receive \$100,000 or more a year in Federal funds to have an audit made for that year. Section 7505 of the Act requires the Director of the Office of Management and Budget to prescribe policies, procedures and guidelines to implement the Act. It specifies that the Director shall designate "cognizant" Federal agencies, determine criteria for making appropriate charges to Federal programs for the cost of audits, and provide procedures to assure that small firms or firms owned and controlled by disadvantaged individuals have the opportunity to participate in contracts for single audits.

4. Policy. The Single Audit Act requires the following:

a. State or local governments that receive \$100,000 or more a year in Federal financial assistance shall have an audit made in accordance with this Circular.

b. State or local governments that receive between \$25,000 and \$100,000 a year shall have an audit made in accordance with this Circular, or in accordance with federal laws and regulations governing the programs they participate in.

c. State or local governments that receive less than \$25,000 a year shall be exempt from compliance with the Act and other Federal audit

requirements. These State and local governments shall be governed by audit requirements prescribed by state or local law or regulation.

d. Nothing in this paragraph exempts State or local governments from maintaining records of Federal financial assistance or from providing access to such records to Federal agencies, as provided for in Federal law or in Circular A-102, "Uniform requirements for grants to State or local governments."

5. Definitions. For the purposes of this Circular the following definitions from the Single Audit Act apply:

a. "Cognizant agency" means the Federal agency assigned by the Office of Management and Budget to carry out the responsibilities described in paragraph 11 of this circular.

b. Federal financial assistance means assistance provided by a Federal agency in the form of grants, contracts, cooperative agreements, loans, loan guarantees, property, interest subsidies, insurance, or direct appropriations, but does not include direct Federal cash assistance to individuals. It includes awards received directly from Federal agencies, or indirectly through other units of State and local governments.

c. Federal agency has the same meaning as the term 'agency' in section 551(1) of Title 5, United States Code.

d. "Generally accepted accounting principles" has the meaning specified in the generally accepted government auditing standards.

e. "Generally accepted government auditing standards" means the Standards For Audit of Government Organizations, Programs, Activities, and Functions, developed by the Comptroller General, dated February 27, 1981.

f. "Independent auditor" means:

(1) a State or local government auditor who meets the independence standards specified in generally accepted government auditing standards; or

(2) a public accountant who meets such independence standards.

g. "Internal controls" means the plan of organization and methods and procedures adopted by management to ensure that:

(1) resource use is consistent with laws, regulations, and policies;

(2) resources are safeguarded against waste, loss, and misuse; and

(3) reliable data are obtained, maintained, and fairly disclosed in reports.

h. "Indian tribe means any Indian tribe, band, nations, or other organized group or community, including any Alaskan Native village or regional or village corporations (as defined in, or established under, the Alaskan

Native Claims Settlement Act) that is recognized by the United States as eligible for the special programs and services provided by the United States to Indians because of their status as Indians.

i. "Local government" means any unit of local government within a State, including a county, a borough, municipality, city, town, township, parish, local public authority, special district, school district, interstate district, council of governments, and any other instrumentality of local government.

j. "Major Federal Assistance Program," as defined by P.L. 98-502, is described in the Attachment to this circular.

k. "Public accountants" means those individuals who meet the qualification standards included in generally accepted government auditing standards for personnel performing government audits.

l. "State" means any State of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, Guam, American Samoa, the Commonwealth of the Northern Mariana Islands, and the Trust Territory of the Pacific Islands, any instrumentality thereof, and any multi-State, regional, or interstate entity that has governmental functions and any Indian tribe.

m. "Subrecipient" means any person or government department, agency, or establishment that receives Federal financial assistance to carry out a program through a State or local government, but does not include an individual that is a beneficiary of such a program. A subrecipient may also be a direct recipient of Federal financial assistance.

6. Scope of audit. The Single Audit Act provides that:

a. The audit shall be made by an independent auditor in accordance with generally accepted government auditing standards covering financial and compliance audits.

b. The audit shall cover the entire operations of a State or local government or, at the option of that government, it may cover departments, agencies or establishments that received, expended, or otherwise administered Federal financial assistance during the year. However, if a State or local government receives \$25,000 or more in General Revenue Sharing Funds in a fiscal year, it shall have an audit of its entire operations. A series of audits of individual departments, agencies, and establishments for the same fiscal year may be considered a single audit.

c. Public hospitals and public colleges and universities may be excluded from State and local audits and the requirements of this Circular. However, if such entities are excluded, audits of these entities shall be made in accordance with statutory requirements and the provisions of Circular A-110, "Uniform requirements for grants to universities, hospitals, and other nonprofit organizations."

d. The auditor shall determine whether:

(1) the financial statements of the government, department, agency or establishment present fairly its financial position and the results of its financial operations in accordance with generally accepted accounting principles;

(2) the organization has internal accounting and other control systems to provide reasonable assurance that it is managing Federal financial assistance programs in compliance with applicable laws and regulations; and

(3) the organization has complied with laws and regulations that may have material effect on its financial statements and on each major Federal assistance program.

7. Frequency of audit. Audits shall be made annually unless the State or local government has, by January 1, 1987, a constitutional or statutory requirement for less frequent audits. For those governments, the cognizant agency shall permit biannual audits, covering both years, if the government so requests. It shall also honor requests for biannual audits by governments that have an administrative policy calling for audits less frequent than annual, but only for fiscal years beginning before January 1, 1987.

8. Internal control and compliance reviews. The Single Audit Act requires that the independent auditor determine and report on whether the organization has internal control systems to provide reasonable assurance that it is managing Federal assistance programs in compliance with applicable laws and regulations.

a. Internal control review. In order to provide this assurance the auditor must make a study and evaluation of internal control systems used in administering Federal assistance programs. The study and evaluation must be made whether or not the auditor intends to place reliance on such systems. As part of this review, the auditor shall:

(1) Test whether these internal control systems are functioning in accordance with prescribed procedures.

(2) Examine the recipient's system for monitoring subrecipients and obtaining and acting on subrecipient audit reports.

b. Compliance review. The law also requires the auditor to determine whether the organization has complied with laws and regulations that may have a material effect on each major Federal assistance program.

(1) In order to determine which major program are to be tested for compliance, State and local governments shall identify in their accounts all Federal funds received and expended and the programs under which they were received. This shall include funds received directly from Federal agencies and through other State and local governments.

(2) The review must include the selection and testing of a representative number of charges from each major Federal assistance program. The selection and testing of transactions shall be based on the auditor's professional judgment considering such factors as the amount of expenditures for the program and the individual awards; the newness of the program or

changes in its conditions; prior experience with the program, particularly as revealed in audits and other evaluations (e.g., inspections, program reviews); the extent to which the program is carried out through subrecipients; the extent to which the program contracts for goods or services; the level to which the program is already subject to program reviews or other forms of independent oversight; the adequacy of the controls for ensuring compliance; the expectation of adherence or lack of adherence to the applicable Laws and regulations; and the potential impact of adverse findings.

(a) In making the test of transactions, the auditor shall determine whether:

- the amounts reported as expenditures were for allowable services, and
- the records show that those who received services or benefits were eligible to receive them.

(b) In addition to transaction testing, the auditor shall determine whether:

- matching requirements, levels of effort and earmarking limitations were met,
- Federal financial reports and claims for advances and reimbursements contain information that is supported by the books and records from which the basic financial statements have been prepared, and
- amounts claimed or used for matching were determined in accordance with OMB Circular A-87, "Cost principles for State and local governments," and Attachment F of Circular A-102, "Uniform requirements for grants to State and local governments."

(c) The principal compliance requirements of the largest Federal aid programs may be ascertained by referring to the Compliance Supplement for Single Audits of State and Local Governments, issued by OMB and available from the Government Printing Office. For those programs not covered in the Compliance Supplement, the auditor may ascertain compliance requirements by researching the statutes, regulations, and agreements governing individual programs.

(3) Transactions related to other Federal assistance programs that are selected in connection with examinations of financial statements and evaluations of internal controls shall be tested for compliance with Federal laws and regulations that apply to such transactions.

9. Subrecipients. State or local governments that receive Federal financial assistance and provide \$25,000 or more of it in a fiscal year to a subrecipient shall:

a. determine whether State or local subrecipients have met the audit requirements of this Circular and whether subrecipients covered by Circular A-110, "Uniform requirements for grants to universities, hospitals, and other nonprofit organizations, have met that requirement;

b. determine whether the subrecipient spent Federal assistance funds provided in accordance with applicable laws and regulations. This may be accomplished by reviewing an audit of the subrecipient made in accordance with this Circular, A-110, or through other means (e.g., program reviews) if the subrecipient has not yet had such an audit;

c. ensure that appropriate corrective action is taken within six months after receipt of the audit report in instances of noncompliance with Federal laws and regulations;

d. consider whether subrecipient audits necessitate adjustment of the recipient's own records; and

e. require each subrecipient to permit independent auditors to have access to the records and financial statements as necessary to comply with this Circular.

10. Relation to other audit requirements. The Single Audit Act provides that an audit made in accordance with this Circular shall be in lieu of any financial or financial compliance audit required under individual Federal assistance programs. To the extent that a single audit provides Federal agencies with information and assurances they need to carry out their overall responsibilities, they shall rely upon and use such information. However, a Federal agency shall make any additional audits which are necessary to carry out its responsibilities under Federal law and regulation. Any additional Federal audit effort shall be planned and carried out in such a way as to avoid duplication.

a. The provisions of this Circular do not limit the authority of Federal agencies to make, or contract for audits and evaluations of Federal financial assistance programs, nor do they limit the authority of any Federal agency Inspector General or other Federal audit official.

b. The provisions of this Circular do not authorize any State or local government or subrecipient thereof to constrain Federal agencies, in any manner, from carrying out additional audits.

c. A Federal agency that makes or contracts for audits in addition to the audits made by recipients pursuant to this Circular shall, consistent with other applicable laws and regulations, arrange for funding the cost of such additional audits. Such additional audits include economy and efficiency audits, program results audits, and program evaluations.

11. Cognizant agency responsibilities. The Single Audit Act provides for cognizant Federal agencies to oversee the implementation of this Circular.

a. The Office of Management and Budget will assign cognizant agencies for States and their subdivisions and larger local governments and their subdivisions. Other Federal agencies may participate with an assigned cognizant agency, in order to fulfill the cognizance responsibilities. Smaller governments not assigned a cognizant agency will be under the general oversight of the Federal agency that provides them the most funds whether directly or indirectly.

b. A cognizant agency shall have the following responsibilities:

- (1) Ensure that audits are made and reports are received in a timely manner and in accordance with the requirements of this Circular.
- (2) Provide technical advice and liaison to State and local governments and independent auditors.
- (3) Obtain or make quality control reviews of selected audits made by non-Federal audit organizations, and provide the results, when appropriate, to other interested organizations.
- (4) Promptly inform other affected Federal agencies and appropriate Federal law enforcement officials of any reported illegal acts or irregularities. They should also inform State or local law enforcement and prosecuting authorities, if not advised by the recipient, of any violation of law within their jurisdiction.
- (5) Advise the recipient of audits that have been found not to have met the requirements set forth in this Circular. In such instances, the recipient will be expected to work with the auditor to take corrective action. If corrective action is not taken, the cognizant agency shall notify the recipient and Federal awarding agencies of the facts and make recommendations for followup action. Major inadequacies or repetitive substandard performances of independent auditors shall be referred to appropriate professional bodies for disciplinary action.
- (6) Coordinate, to the extent practicable, audits made by or for Federal agencies that are in addition to the audits made pursuant to this Circular; so that the additional audits build upon such audits.
- (7) Oversee the resolution of audit findings that affect the programs of more than one agency.

12. Illegal acts or irregularities. If the auditor becomes aware of illegal acts or other irregularities, prompt notice shall be given to recipient management officials above the level of involvement. (See also paragraph 13(a)(3) below for the auditor's reporting responsibilities.) The recipient, in turn, shall promptly notify the cognizant agency of the illegal acts or irregularities and of proposed and actual actions, if any. Illegal acts and irregularities include such matters as conflicts of interest, falsification of records or reports, and misappropriations of funds or other assets.

13. Audit Reports. Audit reports must be prepared at the completion of the audit. Reports serve many needs of State and local governments as well as meeting the requirements of the Single Audit Act.

a. The audit report shall state that the audit was made in accordance with the provisions of this Circular. The report shall be made up of at least:

(1) The auditor's report on financial statements and on a schedule of Federal assistance; the financial statements; and a schedule of Federal assistance, showing the total expenditures for each Federal assistance program as identified in the Catalog of Federal Domestic Assistance. Federal programs or grants that have not been assigned a catalog number-shall be identified under the caption "other Federal assistance."

(2) The auditor's report on the study and evaluation of internal control systems must identify the organization's significant internal accounting controls, and those controls designed to provide reasonable assurance that Federal programs are being managed in compliance with laws and regulations. It must also identify the controls that were evaluated, the controls that were not evaluated, and the material weaknesses identified as a result of the evaluation.

(3) The auditor's report on compliance containing:

- a statement of positive assurance with respect to those items tested for compliance, including compliance with law and regulations pertaining to financial reports and claims for advances and reimbursements;
- negative assurance on those items not tested;
- a summary of all instances of noncompliance; and
- an identification of total amounts questioned, if any, for each Federal assistance award, as a result of noncompliance.

b. The three parts of the audit report may be bound into a single report, or presented at the same time as separate documents.

c. All fraud abuse, or illegal acts or indications of such acts, including all questioned costs found as the result of these acts that auditors become aware of, should normally be covered in a separate written report submitted in accordance with paragraph 13f.

d. In addition to the audit report, the recipient shall provide comments on the findings and recommendations in the report, including a plan for corrective action taken or planned and comments on the status of corrective action taken on prior findings. If corrective action is not necessary, a statement describing the reason it is not should accompany the audit report.

e. The reports shall be made available by the State or local government for public inspection within 30 days after the completion of the audit.

f. In accordance with generally accepted government audit standards, reports shall be submitted by the auditor to the organization audited and to those requiring or arranging for the audit. In addition, the recipient shall submit copies of the reports to each Federal department or agency that provided Federal assistance funds to the recipient. Subrecipients shall submit copies to recipients that provided them Federal assistance funds. The

reports shall be sent within 30 days after the completion of the audit, but no later than one year after the end of the audit period unless a longer period is agreed to with the cognizant agency.

g. Recipients of more than \$100,000 in Federal funds shall submit one copy of the audit report within 30 days after issuance to a central clearinghouse to be designated by the Office of Management and Budget. The clearinghouse will keep completed audits on file and follow up with State and local governments that have not submitted required audit reports.

h. Recipients shall keep audit reports on file for three years from their issuance.

14. Audit Resolution. As provided in paragraph 11, the cognizant agency shall be responsible for monitoring the resolution of audit findings that affect the programs of more than one Federal agency. Resolution of findings that relate to the programs of a single Federal agency will be the responsibility of the recipient and that agency. Alternate arrangements may be made on a case-by-case basis by agreement among the agencies concerned.

Resolution shall be made within six months after receipt of the report by the Federal departments and agencies. Corrective action should proceed as rapidly as possible.

15. Audit workpapers and reports. Workpapers and reports shall be retained for a minimum of three years from the date of the audit report, unless the auditor is notified in writing by the cognizant agency to extend the retention period. Audit workpapers shall be made available upon request to the cognizant agency or its designee or the Federal Accounting Office, at the completion of the audit.

16. Audit Costs. The cost of audits made in accordance with the provisions of this Circular are allowable charges to Federal assistance programs.

a. The charges may be considered a direct cost or an allocated indirect cost, determined in accordance with the provision of Circular A-87, Cost principles for State and local governments.

b. Generally, the percentage of costs charged to Federal assistance programs for a single audit shall not exceed the percentage that Federal funds expended represent of total funds expended by the recipient during the fiscal year. The percentage may be exceeded, however, if appropriate documentation demonstrates higher actual cost.

17. Sanctions. The Single Audit Act provides that no cost may be charged to Federal assistance programs for audits required by the Act that are not made in accordance with this Circular. In cases of continued inability or unwillingness to have a proper audit, Federal agencies must consider other appropriate sanctions including:

- withholding a percentage of assistance payments until the audit is completed satisfactorily,
- withholding or disallowing overhead costs, and

-- suspending the Federal assistance agreement until the audit is made.

18. Auditor Selection. In arranging for audit services State and local governments shall follow the procurement standards prescribed by Attachment O of Circular A-102, "Uniform requirements for grants to State and local governments." The standards provide that while recipients are encouraged to enter into intergovernmental agreements for audit and other services, analysis should be made to determine whether it would be more economical to purchase the services from private firms. In instances where use of such intergovernmental agreements are required by State statutes (e.g., audit services) these statutes will take precedence.

19. Small and Minority Audit Firms. Small audit firms and audit firms owned and controlled by socially and economically disadvantaged individuals shall have the maximum practicable opportunity to participate in contracts awarded to fulfill the requirements of this Circular. Recipients of Federal assistance shall take the following steps to further this goal:

a. Assure that small audit firms and audit firms owned and controlled by socially and economically disadvantaged individuals are used to the fullest extent practicable.

b. Make information on forthcoming opportunities available and arrange timeframes for the audit so as to encourage and facilitate participation by small audit firms and audit firms owned and controlled by socially and economically disadvantaged individuals.

c. Consider in the contract process whether firms competing for larger audits intend to subcontract with small audit firms and audit firms owned and controlled by socially and economically disadvantaged individuals.

d. Encourage contracting with small audit firms or audit firms owned and controlled by socially and economically disadvantaged individuals which have traditionally audited government programs and, in such cases where this is not possible, assure that these firms are given consideration for audit subcontracting opportunities.

e. Encourage contracting with consortiums of small audit firms as described in paragraph (a) above when a contract is too large for an individual small audit firm or audit firm owned and controlled by socially and economically disadvantaged individuals.

f. Use the services and assistance, as appropriate, of such organizations as the Small Business Administration in the solicitation and utilization of small audit firms or audit firms owned and controlled by socially and economically disadvantaged individuals.

20. Reporting. Each Federal agency will report to the Director of OMB on or before March 1, 1987, and annually thereafter on the effectiveness of State and local governments in carrying out the provisions of this Circular. The report must identify each State or local government or Indian tribe that, in the opinion of the agency, is failing to comply with the Circular.

21. Regulations. Each Federal agency shall include the provisions of this Circular in its regulations implementing the Single Audit Act.

22. Effective date. This Circular is effective upon publication and shall apply to fiscal years of State and local governments that begin after December 31, 1984. Earlier implementation is encouraged. However, until it is implemented, the audit provisions of Attachment P to Circular A-102 shall continue to be observed.

23. Inquiries. All questions or inquiries should be addressed to Financial Management Division, Office of Management and Budget, telephone number 202/395-3993.

22. Sunset review date. This Circular shall have an independent policy review to ascertain its effectiveness three years from the date of issuance.

(Signed)
David A. Stockman
Director

Circular A-128
Attachment

Definition of Major Program as Provided
in P.L. 98-502

"Major Federal Assistance Program," for State and local governments having Federal assistance expenditures between \$100,000 and \$100,000,000, means any program for which Federal expenditures during the applicable year exceed the larger of \$300,000, or 3 percent of such total expenditures.

Where total expenditures of Federal assistance exceed \$100,000,000, the following criteria apply:

Total Expenditures of Federal Financial Assistance for All Programs		Major Federal Assistance Program Means any Program That Exceeds
<u>more than</u>	<u>but less than</u>	
\$100 million	\$ 1 billion	\$ 3 million
1 billion	2 billion	4 million
2 billion	3 billion	7 million
3 billion	4 billion	10 million
4 billion	5 billion	13 million
5 billion	6 billion	16 million
6 billion	7 billion	19 million
over 7 billion		20 million

Grants - Assignment of Audit Cognizance For State Agencies

Assignments of Audit Cognizance for State Agencies. The following list shows the assignment of audit cognizance for State and local agencies for which the DOE is currently responsible.

Eastern Region

Illinois - Institute of Natural Resources

Indiana - Department of Commerce

Puerto Rico - Office of Energy

Western Region

Nebraska - Policy Research & Energy Office

New Mexico - Energy, Minerals & Natural Resources Department

REPORT CONTROL LOG FOR COGNIZANT AUDITS
OF STATE AND LOCAL GOVERNMENTAL UNITS UNDER
THE REQUIREMENTS OF OMB CIRCULAR A-128

1. Name of Cognizant Entity: _____
2. Address: _____ Telephone: _____
3. Contact Person at Audited Entity: _____
4. Audit Period: From: _____ To: _____
5. Date of Audit Report: _____
6. Date Audit Report Received by OIG: _____
7. Name of Independent Audit Organization: _____
8. Auditor-In-Charge: _____ Telephone # _____
9. Date OIG Desk Review Completed: _____
10. Distribution of Report by IG Regional Office:

Distributed To:

Date

_____	_____
_____	_____
_____	_____
_____	_____

11. Audit findings identified for resolution by DOE officials, including cross-cutting issues:

12. Dollar Magnitudes:

- a. Total Expenditures \$ _____
- b. Expenditures Audited \$ _____
- c. Expenditures Questioned \$ _____
- d. Questioned Costs Sustained (DOE Only) \$ _____

13. Comments on independent auditor's conclusions about internal control weaknesses; noncompliance with program requirements; and/or significant deficiencies or program weaknesses. (if additional space is needed, use next page.)

14. Reviewer's conclusions as to the acceptability of the independent audit (i.e., does it meet IG audit needs?):

15. If a Quality Control Review needed? Yes ___ No ___ If yes, discuss the plan and the schedule for undertaking additional work. (The reviewer should also contact the OIG regional single audit contact person for any special processing instructions.)

AIIM

Association for Information and Image Management

1100 Wayne Avenue, Suite 1100
Silver Spring, Maryland 20910

301/587-8202

Centimeter

Inches

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6 of 7

REPORT CONTROL LOG FOR NONCOGNIZANT AUDITS
OF STATE AND LOCAL GOVERNMENTAL UNITS UNDER
THE REQUIREMENTS OF OMB CIRCULAR A-128

1. Name of Cognizant Entity: _____
2. Address: _____ Telephone: _____
3. a. Name of Cognizant Audit Agency: _____
b. Contact Person at Cognizant Audit Agency: _____
c. Telephone: _____
4. Audit Period: From: _____ To: _____
5. Date of Audit Report: _____
6. Date Audit Correspondence or Report Received by OIG: _____
7. Distribution of Report by IG Regional Office: _____

Distributed To:

Date

<u>Distributed To:</u>	<u>Date</u>
_____	_____
_____	_____
_____	_____
_____	_____

8. Audit findings identified for resolution by DCE officials:

9. Dollar Magnitudes:

a. Total Expenditures	\$ _____
b. Expenditures Audited	\$ _____
c. Expenditures Questioned	\$ _____
d. Questioned Costs Sustained (DOE Only)	\$ _____

10. Comments on independent auditor's conclusions about internal control weaknesses; noncompliance with program requirements; and/or significant deficiencies or program weaknesses. (if additional space is needed, use next page.)

11. Reviewer's assessment as to the acceptability of the independent audit (i.e., does it meet IG audit needs?):

12. If item 10 is negative, discuss steps that are needed and will be taken to obtain additional information or undertake additional work. (The reviewer should also contact the OIG regional single audit contract person for any special processing instructions.)

CHECKLIST FOR DESK REVIEWS OF COGNIZANT AUDITS
OF STATE AND LOCAL GOVERNMENTAL UNITS UNDER
THE REQUIREMENT OF OMB CIRCULAR A-128

PURPOSE: The objective of a desk review of a single audit is to assure that the audit report meets applicable reporting standards and the single audit reporting requirements. The purpose is sufficient to fulfill the objective and is consistent among cognizant agency audit organizations.

APPLICABILITY: All cognizant agencies performing desk reviews will be required to follow the PCIE desk review checklist. The checklist is in draft form and will be issued for use in CY 1990.

CHECKLIST FOR DESK REVIEWS OF
NONCOGNIZANT AUDITS OF
STATE AND LOCAL GOVERNMENTAL UNITS
UNDER THE REQUIREMENTS OF OMB CIRCULAR A-128

Name of Cognizant Agency: _____

Name of Federal Cognizant
Audit Agency: _____

Name of Independent Audit
Organization: _____

Audit Period: From: _____ To: _____

Date of Audit Report: _____

Date Audit Received by OIG: _____

Date Desk Review Completed: _____

Name of Reviewer: _____

Comments on Results of
Review:

	<u>Yes</u>	<u>No</u>
I. <u>AUDIT OPINION AND FINANCIAL STATEMENTS</u>		
1. Does the report include an opinion as to whether information is fairly stated in all material steps in relation to the basic financial statements taken as a whole?	—	—
2. If yes, was the opinion:		
a. Unqualified?		
b. Qualified, Adverse, or Disclaimed?	—	—
3. If less than an unqualified opinion was rendered, do the exceptions involve DOE funds?		
4. Do the financial statements or associated footnote contain adverse disclosures (disallowed or unsupported costs, contingent liabilities, etc.) relating to DOE funds?	—	—
II. <u>INTERNAL CONTROL</u>		
1. Are adverse internal control matters disclosed which could affect DOE-funded programs?	—	—
2. Does the report contain recommendations relative to observed internal control deficiencies?	—	—
3. Are control weaknesses adequately explained, including actual or potential impact on Federal programs?	—	—
III. <u>COMPLIANCE</u>		
1. Does the report contain an expression of positive assurance with respect to compliance with requirements for tested items and negative assurance for untested items?	—	—
2. Are compliance comments clearly explained and conclusive as to impact?	—	—
3. Does the report include recommendation(s) for corrective action with respect to DOE-funded programs;	—	—
4. Are the recommendations sound?	—	—
5. Are there any significant findings that cross agency lines?	—	—

6. Is there a statement in the report or transmittal letter identifying which agency is responsible for resolution of questioned costs or other audit exceptions?

IV. SUMMARY OF RESULTS OF DESK REVIEW

1. Audit deficiencies noted during the desk review requiring followup with the cognizant audit agency:

2. Findings noted in report requiring followup by contracting officers within DOE:

IV. SUMMARY OF RESULTS OF DESK REVIEW

3. Other comments, including OIG plans and time schedules for performing quality control impact:

UNIFORM QUALITY CONTROL REVIEW GUIDE

PURPOSE: The objective of a quality control review (QCR) of a single audit is to assure that the audit was conducted according to applicable standards and meets the single audit requirements. The purpose of this document is to help assure that the scope of QCRs

- is sufficient to fulfill the objective of a QCR; and
- is consistent among cognizant agency audit organizations.

APPLICABILITY: All cognizant agency audit organizations conducting QCRs of A-128 single audits will be required to follow the PCIE Uniform Quality Control Review Guide. The checklist is in draft form and will be issued for use in CY 1990.

QUARTERLY REPORT ON RECIPIENT ORGANIZATIONS NOT COMPLYING WITH A-128 REQUIREMENTS

Regional Office: _____
Quarter Ended: _____

<u>Name of Recipient Agency</u>	<u>Most Recent Audit Period Covered</u>		<u>Audit Report</u>	<u>Date</u>	<u>Next Scheduled Audit</u>		<u>Significant Problems In Obtaining Timely Audits</u>
	<u>From:</u>	<u>To:</u>	<u>Date</u>	<u>Report</u>	<u>Period</u>	<u>Expected Report Date</u>	

QUARTERLY EXCEPTION REPORT ON
QUESTIONED COSTS

Regional Office: _____
Quarter Ended: _____

Recipient	Date Of	Total DOE			Questioned
<u>Agency</u>	<u>Audit</u>	<u>Expenditures</u>	<u>Within</u>	<u>DOE Costs</u>	<u>Cost</u>
	<u>Report</u>	<u>Audit Period</u>	<u>Questioned</u>	<u>Questioned Costs</u>	<u>Sustained</u>

QUARTERLY EXCEPTION REPORT ON
MATERIAL COMPLIANCE
AND INTERNAL CONTROL WEAKNESSES

Regional Office: _____
Quarter Ended: _____

Recipient <u>Agency</u>	Audit Report <u>Date</u>	Total DOE Expenditures Within <u>Audit Period</u>	Synopsis Of Compliance And Internal Control <u>Weaknesses</u>
----------------------------	--------------------------------	--	---

REPORT OF POTENTIAL FRAUD OR ABUSE SITUATIONS

Submitted By: _____ Date: _____

Yes No

1. Is DOE the Audit Cognizant Agency? _____
2. Does the potential fraud or abuse situation pertain only to DOE Federally Assisted Programs? _____
3. If yes to (2.) list other Federally Assisted Program(s) Affected: _____

4. List non-Federal agencies where programs are affected: _____

5. Briefly describe the nature of and circumstances surrounding potential fraud or abuse findings: _____

6. Indicate the magnitude of suspected fraud or abuse situations (dollar amounts, etc.) _____

7. Is coordination necessary with other audit agencies and/or recipient officials? Y__ N__. If so, list specifically who those parties are: _____

8. What do you recommend be done about the potential fraud/abuse situations? _____

REPORT OF SUBSTANDARD AUDITS

Submitted By: _____ Date: _____

This report should be sent to the OAO whenever significant inadequacies in an audit are disclosed and the auditor does not take corrective action.

1. Name of Recipient Agency _____
2. Name of Audit Organization _____
3. Name of Auditor In-Charge _____
4. How was the inadequacy discovered? _____
(i.e., Desk Review, QCR, or QAR)
5. Describe the nature and significance of the deficient audit work.

6. Have you notified the recipient and non-Federal auditor in writing of the reasons why the work is inadequate, the impact on other agencies, recommendations for resolutions, time frames for accomplishing corrective action, and the consequences if corrective action is not taken? _____
(If so, attach a copy of your letter or memo.) _____

CHAPTER 21PROGRAM FOR AUDITING INTEGRATED AND M&O CONTRACTORSA. SCOPE OF CHAPTER

This chapter introduces section VI of the Audit Manual, which provides standard policies and approaches for auditing the Department's integrated and management and operating (M&O) contractors. Audits of DOE's contractors are performed by both the OIG and contractor internal audit staff, as well as by other audit organizations. Guidance in this chapter is intended to assist the OIG and contractor internal auditors in coordinating their audits, minimizing duplication, and ensuring compliance with professional audit standards. Guidance for Voucher Accounting for Net Expenditures Accrued (VANEA) audits, performance audits, and specific audit objectives by contractor function is provided in chapters 22, 23, and 24, respectively.

B. BACKGROUND

DOE relies heavily on contractors to carry out most of its programs, activities, and functions. Most integrated contractors operate under an M&O contract arrangement. However, not all M&O contractor accounting systems are integrated with DOE.

1. Integrated Contractors. An integrated contractor is one whose costs under a cost-type contract are prefunded by DOE and who is required to maintain a separate and distinct system of accounts, records, documents, and other evidence showing and supporting all allowable costs incurred, revenues or other applicable credits. The system of accounts employed by the contractor must be satisfactory to DOE and in accordance with generally accepted accounting principles consistently applied unless DOE requires the use of an alternate accounting policy or procedure.

The accounts maintained by the contractor for operations under the contract are integrated with those of DOE. At the end of each fiscal year, the contractor is required to submit a VANEA which includes the contractor's certification that the costs claimed represent allowable contract costs. The VANEA forms the basis for the OIG's annual assessment of the contractors' system of accounts and the contractors' allowable cost representations. The policies and procedures for conducting VANEA audits are contained in chapter 22.

2. Management and Operating Contracts. An M&O contract is an agreement under which the Government contracts for the operation, maintenance, or support, on its behalf, of Government-owned or -controlled research, development, special production, or testing establishment wholly or principally devoted to one or more major programs of the contracting Federal agency. This type of contract is characterized by (1) utilization of Government-owned or controlled facilities; (2) the Government's need to maintain a special, close relationship with the contractor and contractor personnel; (3) the work which is

wholly or substantially separate from the contractor's other business, if any; and (4) the close relationship with the Agency's mission and the need for a longterm or continuing arrangement.

C. DOE AUDIT OBJECTIVES FOR INTEGRATED AND M&O CONTRACTORS

For performance audits, DOE objectives for audits of integrated and M&O contractor operations are to determine:

- o whether audited functions are being managed efficiently and effectively, and are operating in accordance with applicable laws, regulations, policies, and DOE contract terms.
- o the extent to which program and project management has provided direction to achieve the desired level of results; and
- o if programs, projects, and other activities are functioning as intended and are accomplishing their stated purpose or objective.

For financial statement and financial related audits, the objectives are to determine:

- o the reliability and usefulness of financial statement information reported to DOE and the reliability of the contractor's allowable cost representations;
- o compliance with laws, regulations, and contract provisions that (a) govern the acquisition, management, and use of resources, or (b) have a material effect on financial information;
- o internal controls are adequate, to prevent, identify and report unallowable and unreasonable costs; and
- o allowable costs are addressed, either through a single audit or as steps within all other audits.

The four general types of audit work to be performed to meet these audit objectives are (1) financial statement, (2) financial related, (3) economy and efficiency, and (4) program audits. These types of audits are described in general terms in chapter 2, pages 2-5 and 2-6. In addition, chapter 22 provides guidelines for assessing the allowability and reasonableness of costs incurred by DOE's integrated contractors, and chapter 23 provides a more detailed discussion of performance audits--i.e., economy and efficiency audits, and program audits.

Recognizing its limited resources to achieve all of the above audit objectives and types of audits, it is the OIG's intent to develop a cooperative audit strategy and to rely to the extent possible on the work of others in order to minimize duplication and maximize audit coverage of DOE's integrated and M&O contractors. However, in order for this cooperative strategy to succeed, the OIG must be able to obtain assurance that such audit work meets professional audit standards and other requirements. Also, procedures must be in place to ensure that audit work is planned, coordinated, conducted and reported in an effective and timely manner.

D. ASSURING COMPLIANCE WITH PROFESSIONAL STANDARDS

The OIG can rely on audit work performed by contractor internal audit staffs as long as it can obtain assurance that this audit work meets professional audit standards and other requirements. In general, this assurance will be obtained by reviewing external (peer) reviews and field office appraisals, and by OIG review of internal audit work.

1. External (Peer) Reviews. In accordance with standards established by the Institute of Internal Auditors, external reviews of a contractor internal audit department should be conducted at least once every three years to appraise the quality of the department's operations. These reviews should be performed by qualified persons who are independent of the organization and who do not have either a real or an apparent conflict of interest. These reviews should also assess how well the contractor internal audit staffs comply with contractual audit requirements, normally the standard internal audit clause required by DOE's Acquisition Regulations (DEAR), and with applicable professional audit standards.

To clarify the requirements of the standard audit clause (DEAR 970.5204--9h) and to ensure uniform implementation throughout the Department, DOE Acquisition Letter (AL) 90-3 requires internal audit staffs to be (1) independent, (2) of sufficient size and with appropriate training to meet standards established by the Institute of Internal Auditors, (3) perform financial and performance audits, (4) use program guidance developed by the OIG, (5) prepare annual audit plans, and (6) provide an annual audit report.

2. Appraisals. DOE Order 2321.1B requires the Heads of Field Organizations to appraise the internal audit activities of DOE integrated contractors under their jurisdiction. Specifically, the field office is required to evaluate the adequacy of coverage, technical competency, objectivity, independence and the work performed by internal audit staffs.

3. OIG Reviews. Review of other appraisals or external reviews should aid the OIG in deciding the extent to which reliance can be placed on audit coverage provided by contractor internal audit staffs. However, the OIG also needs to assess the work of internal audit staffs. This assessment should determine whether the work was done in accordance with professional auditing standards and that it met the objectives as outlined in chapters 22, 23 and 24 of the Audit Manual.

E. PLANNING, SCHEDULING AND TRACKING CONTRACTOR AUDITS

The OIG is responsible for developing an annual DOE-wide audit plan by using a risk assessment methodology which considers, among other factors, requests and recommendations for audit coverage from various officials within the Department. To avoid unnecessary duplication in audit coverage, the OIG coordinates with organizations having related functions, such as the GAO, DOE Headquarters, field offices and contractor internal audit organizations.

1. Audit Planning and Risk Assessments. The OIG and contractor audit plans should be based on risk assessment. Risk assessment by appropriate audit organizations will facilitate the best use of available audit resources.

Audit plans based on acceptable risk assessment methodologies should provide adequate audit coverage over those areas most susceptible to waste, fraud and abuse. This risk assessment should include attributes such as adequacy of internal controls, length of time since last audit, dollar value/materiality, changes of systems, and results of prior audits. In addition, the audit organization utilizing this chapter should apply their own risk assessment which reflects their organization's unique needs, considerations, and requirements. The intent is to provide audit coverage over vulnerable areas on an annual basis. Additionally, the OIG and internal audit staffs should document their risk assessment process and reasons for classifying functional areas as having low or no risk.

a. Contractor Internal Audit Risk Assessments and Plans - More detailed guidance for how contractor internal audit groups should assess risk and develop annual audit plans is provided in exhibit A (A:AM21EXA.WPF). Internal audit staffs should provide annual audit plans to their appropriate field office or contracting activity and OIG representative by July 15 of each fiscal year.

b. OIG Risk Assessments and Plans - Chapter 5 discusses the overall OIG audit planning process. However, to ensure appropriate audit coverage of each integrated and M&O contractor, OIG audit directors are responsible for establishing an overall audit plan for each contractor based on the risk assessment methodology illustrated in exhibit B, (A:AM21EXB.WPF). This risk assessment will ensure scheduling of specific performance, financial statement and financial related audits, as appropriate, for each contractor. Also, the OIG will provide planning guidance to the contracting activities and internal audit groups by May 15 for consideration during preparation of the contractor's annual audit plans.

2. Scheduling Audits of Integrated & M&O Contractors. The OIG's overall audit objective is to provide comprehensive audit coverage by scheduling specific financial, financial related, and performance audits of Departmental programs, projects, functions, and activities. The audits scheduled should be based on the risk assessment methodologies described above and not on an arbitrary cycle or timeframe. Additionally, the OIG has agreed that the Defense Contract Audit Agency and other audit organizations will provide coverage for cost audits at some non-integrated M&O contractors. Exhibit C (A:AM21EXC.WPF) discusses agreed upon audit office responsibilities for various non-integrated M&O contractors.

a. Financial and Financial Related Audits - Chapter 22 contains the policy and approach for signing the VANEAs, an audit program for conducting a single allowable cost audit, and scheduling requirements for the VANEAs assessment. Additional financial or financial related audit work should be programed to address the functional areas and audit objectives identified in chapter 24. However, no specific timeframes are required. Rather, audits should be scheduled based on the results of the risk assessments.

b. Performance Audits - No specific schedule or cycle is mandated for completion of performance (program) audits as presented in chapter 23. However, each contractor internal audit group should attempt to perform at least one such audit annually at each contractor location. Additional performance audits should be scheduled based on the results of the risk assess-

ments and as audit resources are available to address the economy and efficiency or program audit objectives for the functional areas identified in chapter 24.

3. OIG Audit Tracking System. The OIG will establish and maintain an Audit Tracking System to provide the information required to coordinate the foregoing activities and to allow the OIG to take full advantage of other entities' audit work in developing its own audit plans, schedules and resource requirements. System information is to be obtained from various sources-- e.g., OIG, Field Offices, Internal Audit staffs, and GAO. The OIG Audit Tracking System will provide information on planned audits and actual audit results performed at integrated and M&O contractor sites. Audit Directors are responsible for inputting, updating and reporting this information. In addition, Audit Directors will assess each audit report and determine if the audit work met OIG objectives for a functional area, as presented in chapter 24.

Access to the system is limited to the OIG, although reports of audit activities will be made available to field office and contractor internal audit staffs. Actual audit findings, results and recommendations will be used by the OIG to assist in their risk assessments but will not be available to the Internal Audit staffs. Exhibit D (A:AM21EXD.WPF) details the OIG Audit Tracking System and provides a suggested report format for the contractor annual audit plans.

Throughout the fiscal year, the field office IG liaison personnel will keep the OIG informed about the audit activities of the contractor internal audit staffs. Copies of all audit reports prepared by the contractor internal auditors will be submitted to the local OIG audit director or to the appropriate regional audit office. The contractor internal audit groups are expected to provide an annual report to their contracting activity and the OIG by January 31 that covers their audit activities during the prior fiscal year.

The coordinated planning efforts of the OIG and internal audit staffs should improve day-to-day communications. A review of audit results by an OIG representative for inclusion in the tracking system should enable the OIG to expand his reliance on the work of others.

AUDIT PLANNING AND RISK ASSESSMENTS

An Annual Audit Plan is the Internal Audit's annual activities schedule. In order to make the best use of audit resources, it is suggested that a risk analysis be performed and documented to determine which areas audits will be accomplished. The plan provides coverage of those areas most vital to the conservation and profitable employment of plant assets, and to the protection of the Department of Energy interests. This risk analysis should consider the entire audit universe for the M&O contractor.

The number of auditable units that comprise our audit universe coupled with limited audit resources prohibits us from performing audits of all auditable units. Consequently, we must review and evaluate the risk associated with each of the auditable units in order to determine where the audit function's efforts should be concentrated. The following areas are essential in the determination of the risk level for the audit universe.

Quality of Internal Controls. This category includes both internal accounting controls and the control environment. The former consists of an entity's accounting system and specific controls. An effective accounting system includes the methods and procedures an entity has to identify, accumulate, classify, analyze, record and report its transactions including possible unallowable costs, and maintain accountability for the related assets. The specific controls are the particular policies and procedures relating to the processing of transactions that management has established to provide assurance its objectives will be achieved, e.g., proper authorizations, adequate segregation of duties, adequate physical controls, etc.

Management's attitude towards controls and its philosophy and operating style affect the control environment. A good understanding of controls by management along with management's strong support for controls are necessary elements of a strong control environment.

Financial Exposure/Materiality. The two pieces that comprise this factor are materiality and the economic environment (state of the economy and congressional direction). In determining financial exposure, primary consideration must be given to how significant the dollar amount is. Consideration should be given to the significance in relation to the particular entity; i.e., legal entity, operational unit, reporting unit, etc. In prioritizing the audits to be performed, financial exposure will be a significant factor.

Results of Last Audit. The results of the last audit by internal audit or the DOE/OIG has a significant influence on the requirements to reassess the function. If the former review indicates a strong control environment, a subsequent review may be postponed in order to concentrate audit resources in another area.

New or Changing Controls, Systems, Program, or Operations. A function's existing and future operating characteristics need to be considered in performing risk assessment. If existing operations are complex, there is more room for error or failure to accurately report results of the ac-

tivities of the organization. A change in management's philosophy without adequate internal controls being established could lead to undesirable results. Reorganization of responsibilities and activities could increase the potential for transactions to be reported and recorded incorrectly or not at all.

Time Since Last Audit. A function that has not been audited by internal audit has a much higher risk of control weaknesses than one that has been reviewed on an annual basis.

Individual M&O contractors may add other areas of risk exposure which apply to the site. Each of the identified areas of risk exposures should then be assigned a risk weight factor. Both the risk exposures and weight factors may vary from year to year and should be evaluated annually.

The next step is to determine for all auditable entities in the identified audit universe what level of risk they currently have. This should be on a consistent numeric scale. This rating of risk exposures is a difficult and time-consuming task. The level of exposure for each area of risk is determined as it applies to a particular auditable entity. The risk rating is then multiplied by its associated risk weight factor. The resulting risk factor scores are added to obtain a risk factor total. This total is a numeric representation of the risk exposure for a given auditable entity with the highest score representing the highest exposure/vulnerability.

Audit topics selected for review, depth, and breadth of coverage are dependent primarily on the resources made available to the internal audit office, particularly the quantity and quality of manpower. Care will be exercised to achieve an optimum balance between the breadth and/or frequency of coverage in any one area and the number of areas to be audited. If the risk ranking process is used for audit selection it will provide documentation supporting internal audit decisions for audit coverage.

The following example illustrates how the suggestions listed above could be applied. For further information, see the professional periodical, the Internal Auditor, issue of June 1983 containing the article entitled, "Audit Project Evaluation Methodology", by O. Ronald Gray, PhD, CIA, CDA CMA.

M&O CONTRACTOR, INC
INTERNAL AUDIT DEPARTMENT
FISCAL YEAR XX RISK ANALYSIS

INDIVIDUAL WEIGHT FACTORS OF RISK EXPOSURE/POTENTIAL RISK FACTORS

AUDIT TOPIC	CORE AUDIT	IG/DOE REQUEST	MGMT. REQUEST	2	5	4	1	3	TOTAL RISK VALUE	TOTAL EST. AUDIT DAYS
				NEW OR CHANGING CONTROLS, SYSTEMS PROGRAM OR OPERATIONS	FINANCIAL EXPOSURE	RESULTS OF LAST AUDIT	TIME SINCE LAST AUDIT	QUALITY OF INT. CONTROLS		
FINANCIAL MANAGEMENT										
Financial Acctg./Fiscal Year End	*			1	2	3	1	3	Req'd	130
Cash Management	*			2	4	2	3	3	44	
Accounts Payable	*			1	3	3	5	3	43	
Accounts Receivable	*			1	3	4	5	4	50	
Property Accounting	*			1	1	3	4	2	29	
Reimbursable Accounting	*			4	5	3	4	4	61	20
Financial Accounting/Reporting	*			2	5	3	4	4	57	
Payroll	*			5	5	4	2	5	68	30

* Use Tracking Codes in Chapter 24

- 1 = Very Low Exposure
- 2 = Moderately Low Exposure
- 3 = Neutral Rating
- 4 = Some Exposure
- 5 = High Exposure

IG RISK ASSESSMENT METHODOLOGY

The OIG is responsible for auditing DOE integrated and M&O contractor activities. Addressing a multitude of issues at numerous activities requires a coordinated planning structure based on a risk assessment methodology. The following is a suggested risk assessment approach that considers all integrated and M&O contractor functions, and integrates internal audit staff plans and OIG initiatives.

AUDIT PLANS

Audit plans based on risk assessments require the entire audit universe to be identified, risk areas developed, and risk levels assigned for each risk area and element in the audit universe. The numeric total for each function can then be compared to identify the highest areas of risk.

Audit plans should be based on a risk assessment for each integrated and M&O contractor. With such assessments, the entire audit priority planning process will be fully documented. If a subsequent challenge is made of the audit plan, audit management should be in a good position to argue that a good faith attempt was made giving full consideration to both tangible and intangible variables. (see The Internal Auditor/June 1983, Article by O. Ronald Gray, PHD, CIA, CPA, Internal Auditor/CMA, entitled "Audit Project Evaluation Methodology").

AUDIT UNIVERSE

The audit universe for risk assessment purposes are the functions as outlined in chapter 24.

RISK AREAS

The following are the OIG risk areas and assigned numeric values:

- o Inspector General Initiatives (11)
- o Financial Exposure/Materiality (10)
- o Results of Prior OIG Audits (9)
- o Results of Internal Audits (8)
- o Strength of Internal Audit Function (7)
- o Results of Other Audits (6)
- o Risk Assessment Prepared by Internal Audit Staffs (5)
- o Contract Modifications, Changes in Internal Controls, Systems, Programs Personnel (4)
- o IG Hotline (3)
- o Time Since Last Internal Audit (2)
- o Time Since Last OIG Audit (1)

Risk Levels. The following are the OIG risk levels and assigned numeric value.

- o Very Low Exposure (1)
- o Moderately Low Exposure (2)
- o Neutral (3)
- o Some Exposure (4)
- o High Exposure (5)

The following example illustrates the suggested risk ranking assessment process.

IG RISK ASSESSMENT

FINANCIAL MANAGEMENT

	Weight Factor A	Weight Factor B	Etc.	Etc.	Etc.	Etc.	Etc.	Etc.	Etc.	Etc.	Etc.	*Total Risk Value
	7	5	11	10	8	9	6	4	3	1	2	
Financial Accounting & Year-End Review	2	3	4	1	2	2	2	3	1	4	1	150
Cash Management				5								
Accounts Payable				2								
Accounts Receivable				1								
Property Accounting				4								
Reimbursable Accounting				4								
Financial Accounting & Reporting				3								
Payroll				3								
Travel				4								
Cost Distribution System				2								

Procurement

Etc.
Etc.
Etc.

Risk Exposure:

- 1-Very Low Exposure
- 2-Moderately Low Exposure
- 3-Neutral Rating
- 4-Some Exposure
- 5-High Exposure

* Total equals (Weight Factor A x Risk Levels)+
(Weight Factor B x Risk Level)+
Etc.

Example (7x2)+(5x3)+(11x4)+(10x1)+(8x2)+(9x2)+(6x2)+
(4x3)+(3x1)+(1x4)+(2x1)=150

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
AUDIT OPERATIONS
DOE'S NON-INTEGRATED MANAGEMENT AND OPERATING CONTRACTORS
AUDIT COVERAGE--COST AUDITS

<u>CONTRACTOR</u>	<u>FACILITY</u>	<u>LOCATION OF G&A RECORDS</u>	<u>PREVIOUS AUDIT COVERAGE</u>	<u>FUTURE INDIRECT COST AUDITS COVERAGE</u>	<u>FUTURE DIRECT COST AUDITS COVERAGE</u>
1. LOVELACE BIOMEDICAL	INH TOXICOLOGY RES.	FACILITY	DOE-OIG	DOE-OIG	DOE-OIG
2. ROSS AVIATION	AIR TRANSPORT SERV.	FACILITY	DOE-OIG	DOE-OIG	DOE-OIG
3. SOUTHEASTERN UNIVERSITIES	CEBAF	FACILITY	DOE-OIG	DOE-OIG	DOE-OIG
4. UNIVERSITY OF GEORGIA	SR. ECOLOGY LAB.	FACILITY	HHS	HHS	HHS*
5. WACKENHUT	NEVADA GUARD SERV.	FL-HOME OFC.	DOE-OIG	DCAA	DOE-OIG
6. WACKENHUT	SAVANNAH RIVER GUARD	FL-HOME OFC.	DCAA	DCAA	DOE-OIG
7. WACKENHUT	ROCKY FLATS GUARD	FL-HOME OFC.	N/A	DCAA	DOE-OIG
8. UNIVERSITY OF CALIF.	BASIC RADIOBIOLOGICAL	FL-HOME OFC.	DOE-OIG	DOE-OIG	DOE-OIG

AUDIT POLICY

- DOE-OIG WILL BE RESPONSIBLE FOR ALL PERFORMANCE AUDITS, AND HAS AUDIT COGNIZANCE FOR ALL DOE M&O CONTRACTS.
- M&O CONTRACTORS WITH GENERAL AND ADMINISTRATIVE (G&A) RECORDS LOCATED AT THE HOME OFFICE. DOE CONTRACTING OFFICER WILL REQUEST DCAA TO DO INDIRECT COST INCURRED AUDITS.
THE DOE-OIG WILL ASSUME RESPONSIBILITY FOR ALL AUDITS OF DIRECT COST INCURRED AT THE FACILITY.
- M&O CONTRACTORS WITH G&A RECORDS LOCATED AT THE DOE FACILITY.

THE DOE-OIG WILL BE RESPONSIBLE FOR THE DIRECT AND INDIRECT AUDITS.

- DCAA HAS ASSUMED RESPONSIBILITY FOR FURNISHING CONTRACT AUDIT SERVICES FOR DOE, THAT INCLUDES DOE PRIME CONTRACTS AND SUBCONTRACTS. HOWEVER, DOE-OIG RETAINED AUDIT COGNIZANCE FOR ALL CONTRACTS AT PRINCETON.

* THIS IS THE COGNIZANT AUDIT AGENCY. INCLUDES A-128 AUDIT COVERAGE.

IG AUDIT TRACKING SYSTEM

The IG Audit Tracking System is part of the current IGDBMS. Data input and retrieval is limited to authorized personnel. Complete Audit Tracking System operating instructions are available in the DBMS.

AUDIT TRACKING DATA REQUIREMENTS

The IG Audit Tracking System contain the following data fields. Unless otherwise noted these fields are required for each audit record.

External Audit Number	Audit number assigned by auditing organization.
Internal Audit Number	Audit Number assigned by the IG Audit Director.
IG Office	IG Field Office responsible for M&O oversight or office performing the audit.
M&O Contractor	M&O Contractor Identifier. (Input by IG.)
Audit Title	Brief description of audit.
Planned Staff Days	Number of staff days budgeted for the audit.
Actual Staff Days	Number of actual staff days to perform audit. (IG Audit only.)
Audit Group	Name of agency performing the audit.
Planned Start Date	Month, Day, Year of planned start date of audit-use report issue date.
Planned End Date	Month, Day, Year of estimated completion date of audit-use report issue date.
Actual Start	Date of opening conference. (IG Audits Only.)
Audit Findings	Brief summary of each finding, result and recommendation in the audit report. This data is input by the Audit Director from the audit report.
Report Date	Month, Day, Year report issued.
Risk Factor	Audit risk indicator based on audit finding and recommendations. Input by IG and used for IG annual audit planning and risk assessment.
Audit Tracking Code -Budget	Four digit audit objective code as identified in the IG Audit Manual, Chapter 24.
Audit Tracking Code -Actual	Four digit audit objective code. Audit Director inputs based on report findings.

Audit Objective Met? Yes/No determination made by Audit Director for each audit objective.

AUDIT TRACKING REPORTS

The following reports are available:

M&O Contractor by Audit Area.

M&O Contractor by Audit Objective.

Summary information is available through on-line report screens. On-Line retrieval may be accessed using the following data fields.

By Internal Audit Number

By M&O Contractor and External Audit Number

BY M&O Contractor and Audit Title

FORMAT FOR CONTRACTOR AUDIT PLAN SUBMISSION

The Contractor Annual Audit Plan submitted to the designated DOE field official and cognizant Office of the Inspector General no later than July 15 of each year should contain the following information:

1. List of audit areas in risk ranked sequence and documentation to support the M&O Contractor's risk assessment methodology.
2. Documentation of the methodology used for auditing the allowability of costs - Single audit or step within each audit.
3. Annual Audit Plan which includes:

Contractor assigned audit number

Audit Title

Planned Staff Days

Planned Start Date

Planned End Date

Audit Tracking Codes - Budget (List the codes for all objectives which will be covered in the audit.)

EXAMPLE: AUDIT PLAN REPORT FORMAT

M&O CONTRACTOR AUDIT PLAN FOR FY 19XX

<u>AUDIT</u> <u>NUMBER</u>	<u>AUDIT TITLE</u>	<u>STAFF</u> <u>DAYS</u>	<u>PLANNED</u> <u>START</u>	<u>PLANNED</u> <u>END</u>	<u>AUDIT</u> <u>TRACKING CODES</u>
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CHAPTER 22OIG VANEA ASSESSMENT OF INTEGRATED CONTRACTORSA. SCOPE OF CHAPTER

This chapter sets forth general guidelines for satisfying the OIG's VANEA audit responsibilities.

B. BACKGROUND

Contractors, whose costs DOE prefinances through letters of credit or cash advances, and which operate or otherwise use Government-owned facilities and resources, maintain financial accounts which are normally integrated with DOE's accounting system. Periodic audit of the accounting controls, transactions, and account balances, as well as the financial reports prepared by the integrated contractors, is an integral part of the OIG's assessment of the allowability and reasonableness of costs incurred by DOE's integrated contractors.

Financial statements are prepared according to the format prescribed by DOE. At the close of each fiscal year, each integrated contractor formally accounts for the net expenditures accrued for the year on a form entitled Voucher Accounting for Net Expenditures Accrued (DOE Form CR-348). This form summarizes the accounting results for the net expenditures accrued during the fiscal year. The total equals the contractor's net disbursements, plus the changes in assets. Contractually, integrated M&O contractors are also required to certify on the VANEA that the VANEA was "prepared in accordance with DOE reporting requirements, from records maintained in conformity with generally accepted accounting principles, and the net expenditures accrued have been incurred and in our opinion are allowable under the contract." Allowable cost provisions and cost prohibitions are normally specified in the contract. Guidance to the Contracting Officer for determining allowable contract costs under M&O contracts is contained in Department of Energy Acquisition Regulation (DEAR) 970.31, Contract Costs Principles and Procedures.

C. POLICY AND APPROACH TO SIGNING THE VANEA

This section provides policies related to signing the VANEA, policy references, general audit approach, performance requirements, and reporting guidance.

1. Policy on Signing the VANEA. Audit Directors will, by March 1, sign and return to the Field Element the VANEA for the previous fiscal year in accordance with the following guidance:

- o The VANEA will only be signed if the contractor's Internal Audit Group performed either a single audit (performed) or steps within each audit program over a five year period that sufficiently tested the contractor's internal controls over costs. Whatever option is chosen, sufficient transaction testing of incurred costs will be performed to ensure that they were reasonable and allowable under

contract terms. All costs identified as unallowable must have been quantified and appropriate adjustments made to the VANEA. Additionally, internal controls relating to allowability of costs deficiencies must have been reported and appropriate corrective actions taken.

- o The VANEA signature will be supported by the work discussed in the "approach."
- o The internal auditors allowable cost audit can be a single audit or steps within all other audit programs performed over a five year period as long as the universe of unallowable costs is identified and covered over that period. If a single audit approach is selected, SAMPLE AUDIT PROGRAMS ARE SHOWN IN EXHIBITS A AND B.

2. VANEA Policy References. The following DEAR provisions and DOE Orders apply to the VANEA policy:

- o DEAR 942.002 - defines Department's responsibility to monitor M&O contractors.
- o 970-5204-9 - requires M&O contractors to perform internal audits of costs claimed to be allowable costs as clarified by DOE Acquisition Letter 90-3R; the most recent version.
- o 970-5204-13 - defines allowable and unallowable costs.
- o 970-5204-15 - limits payment by Government.
- o 970-5204-16 - requires M&O to submit VANEA annually.
- o 970-3101-4 - determines costs based on audits.
- o 970-7103-00 - specifies contractor purchasing systems for assuring compliance with DOE requirements.
- o DOE Order 2200.8B, chapter 1, paragraph 3.c.(3) - sets forth responsibilities for review and approval of VANEA.
- o DOE Order 2321.1B - sets OIG audit responsibilities.

3. Approach to VANEA Auditing. The Department carries out its multi-purpose mission through M&O contracts with commercial concerns, educational institutions, and nonprofit organizations.

The integrated contractor is required by its contract to annually prepare and certify a VANEA based on audit work performed by internal audit staffs or others. The form serves as the contractor's claim and certification that the net expenditures accrued have been incurred and are allowable under the contract. The form also provides for DOE's approval of the contractor's accounting for net expenditures accrued subject to any adjustments noted by future audits. A copy of the DOE approved VANEA is returned to the contractor.

Chapter 1 of DOE Order 2200.8B specifies the division of responsibility for approving the VANEA. Under the order, the integrated contractor's internal audit staff, or others periodically examines the reliability of the internal controls used by the contractor to assure that only costs allowable under terms of the contract are claimed and reimbursed. This review includes an examination of related internal controls and sufficient testing of costs incurred to establish contractor compliance with the contract's allowable cost provisions and any pertinent advance agreements. The Finance Director confirms that the contractor maintained an adequate and approved accounting system, and attests that the contractor's accounting for net expenditures accrued conforms with generally accepted accounting principles, and does not conflict with the provisions of the accounting directives.

The OIG will meet its VANEA responsibilities by annually assessing changes to the contractors internal control structure to assure that costs claimed (supported by accounts and records) and reimbursed by DOE are allowable under the contract, and the work of integrated contractor's internal audit staffs.

The OIG's internal control assessment should include, but not necessarily be limited to, the following:

- Internal Control System Changes,
- Contract Terms,
- Audit Reports by the OIG and Other Entities, and
- Other Information Determined to be Relevant. (See Ex. C.)

If there were no changes or if the changes that occurred were benign, the assessment would result in a negative report. If, on the other hand, changes occurred that were adverse or if the internal control system was not changed to correct an adverse condition reported in an audit report, then the assessment would result in a reported condition.

The OIG assessment of the internal auditor's work should include, but not necessarily be limited to, the following:

- Internal Audit Staff Qualifications,
- Independence of Internal Audit Function,
- Acceptability of Internal Auditor's Work, including
 - Internal Audit's Risk Assessment,
 - Internal Audit's Approach to Conducting Allowable Cost Audits, and
 - Internal Audit Staff Reports and Workpapers.
- Tests to Verify the Accuracy of Internal Audit Conclusions. (See Ex. D.)

4. Performance of VANEA Audits. The internal auditor's allowable cost audit(s) and OIG assessments for each fiscal year will be completed no later than five months (March 1) following the end of the fiscal year reviewed. The VANEA audit will be performed as described above. The approach, whichever adopted by the internal audit staff, should be adjusted to reflect the uniqueness of contractor activities, and be the result of a risk assessment associated with costs incurred during performance of these activities (see exhibit A, A:AM22EXA.WPF, for a sample audit program).

5. Year End Financial Review. The auditor should perform a year end financial account review which analyses year end entries, compliance with applicable contract cost provisions, cost accounting standards, and a cursory check for unusual entries. The auditor should also reconcile the VANEA voucher numbers to the general ledger.

6. OIG Reporting Requirements. The OIG will report the results of their annual assessments of internal controls and internal audit staffs in accordance with Exhibits E (A:AM22EXE.WPF) and F (A:AM22EXF.WPF). The Report on the Assessment of Changes in Internal Controls will be attached to the VANEA. The Report on the Assessment of Internal Audit will be issued as a separate report.

In addition, the VANEA should be footnoted at the OIG signature block so as to refer the reader to the OIG report that accompanied the VANEA sent to the Finance Director, regardless of whether the VANEA is signed by the authorized OIG audit official. (Whether signed or not, a copy of the VANEA should also be sent to the DAIG/AO. If an unsigned VANEA is subsequently signed, a signed copy should also be forwarded to the DAIG/AO.) The signing of the VANEA is solely dependent on what kind of audit opinion can be rendered on the adequacy of the system from which integrated contractor statements were prepared. If the audit opinion rendered is other than unqualified, the VANEA finding(s) should be incorporated into the OIG annual FMFIA report to management for the current year. It should be noted that if the contractor's internal audit activity is judged to be ineffective because of insufficient audit coverage, a disclaimer of VANEA opinion can be made. For a summary of the Levels of Expression of Opinion on a VANEA, see EXHIBIT G (A:AM22EXF.WPF). EXHIBIT H (not on disk) contains a copy of the VANEA form.

When approved by the OIG audit director and the DOE finance officer, the voucher provides the basis for reducing the balance in the contractor's current account by the amount of the net expenditures accrued and for a reciprocal entry on the books of the field office. Such approval also constitutes acknowledgment by DOE that the net expenditures accrued represent allowable contract costs. It is to be noted, however, that such "approved" costs may be further adjusted in the event a later audit discloses unallowable additional costs which were not disclosed by audits performed to date (See DEAR 970.5204-16 (e), Review and Approval of Costs Incurred).

- a. Transmittal Letter - See chapter 11 for a sample transmittal letter.
- b. Report Cover - VANEA reports will normally have a cover similar to that for Blue and Buff Cover reports, but printed on orange paper. Refer to chapter 10 for an example.
- c. Title Page and Table of Contents - The title page and table of contents should be essentially the same as those for Blue and Buff Cover reports, modified as appropriate. Refer to chapter 10 for examples.
- d. Assessment Objectives - The signature on the voucher of the authorized representative of the OIG means that sufficient professional work was done to support that approval signature. To achieve this, the assessment

will consist of, at a minimum, those items identified in 3 above. These assessments will be performed by OIG auditors. The total knowledge and confidence gained from this overall assessment plus the performance audits will provide the necessary assurance that the amounts shown on the voucher are correct or must be adjusted as reported by the auditors.

Chapter 24 displays those functions typically found at an integrated contractor's site. Audit coverage under financial accounting and reporting includes yearend financial account review. Essentially, this review requires an analysis of yearend entries, compliance with applicable contract cost provisions, cost accounting standards, and a limited check for unusual entries.

The Regional Offices and Office of Audit Operations will track the results of the internal auditors' reviews of financial accounts, cost accounting and distribution systems and OIG reviews. All audit finding follow-up systems should also be periodically queried to ensure the timely and comprehensive correction of reported findings.

Completion of the assessments will provide the necessary basis for OIG approval and certification of the voucher. Since ultimate certification of the voucher depends on the composite audit coverage of many Federal and contractor reviews, it is incumbent on all parties to coordinate audit schedules, approaches, and scope to ensure an overall quality product for the Department.

SAMPLE AUDIT PROGRAM
ALLOWABLE COST AT
MANAGEMENT AND OPERATING CONTRACTORS

PURPOSE AND OBJECTIVE

The purpose of this audit is to review the M&O's compliance with the allowable cost provisions of the contract.

The objective of this audit is to determine if the M&O claimed unallowable costs.

AUDIT SCOPE

This audit will be accomplished by:

- Obtaining the criteria for determining the allowability of cost for the specific M&O.
- Reviewing the contractor's internal controls designed to ensure that only allowable costs are claimed under the contract; and
- Testing transactions to determine if unallowable costs were claimed.

AUDIT STEPS

A. Criteria.

In order to evaluate internal controls over allowable costs and to review costs for allowability, the auditor must first ascertain the criteria against which the costs will be measured. Determining criteria for allowability is the key to auditing for allowable cost. Therefore, the auditor must identify and become familiar with the criteria for determining the allowability of cost at the M&O.

Appendix A of this program was developed to test transactions for cost allowability. The tests in appendix A should be adjusted to conform to the criteria for the specific M&O.

1. Brief the contract and any modifications that were in effect during fiscal year(s) being reviewed. This brief will include all contract terms, provisions, and appendices that could have an impact on the determination of cost allowability. The brief should also include contract terms with which noncompliance could result in unallowable cost.

2. Obtain in writing from the contracting officer, a listing of all laws, regulations, rulings, contracting officer decisions, and other agreements that could have an impact on the determination of cost allowability. These documents should be briefed.

3. Identify the Cost Accounting Standards (CAS) requirements of the

contract.

4. If the contract requires CAS compliance, determine if:
 - M&O has filed an up-to-date CAS disclosure statement,
 - DOE has reviewed the disclosure statement and issued an adequacy statement,
 - DOE has reported on the M&O's compliance with CAS, and
 - M&O's disclosure statement describes how the M&O identifies, accumulates, and reports unallowable costs.

B. Internal Controls.

1. Obtain an understanding of the M&O's applicable internal controls in effect during the fiscal year(s) being reviewed. Applicable internal controls are those internal controls that ensure that the M&O did not claim unallowable costs.

2. Document this understanding of the controls.

3. Evaluate whether controls are in place by:

a. Walking-through a selection of transactions in each major control system, and

b. Interviewing the key personnel for each major control system.

4. Assess the risk that the M&O could incur and claim unallowable costs. This assessment should consider inherent risk (i.e. probability that cost category contains unallowable costs) and control risk (i.e. whether the controls are adequate to detect and prevent unallowable costs).

5. Document the conclusions reached in this risk assessment.

C. Accounting for Unallowable Costs.

1. Obtain an understanding of and document the M&O's policies, procedures, and systems for costs which the M&O's internal controls identified as unallowable.

a. Document account names, numbers, and descriptions, type of costs charged, and whether the M&O actually uses the accounts to accumulate unallowable cost.

b. Determine what funding the M&O uses to pay for these identified unallowable costs.

c. Document the transaction flow for unallowable costs to deter-

mine if the M&O pays directly for the cost or if it is first paid through the DOE letter of credit.

2. Verify that unallowable costs identified by the M&O were not reimbursed by DOE or other Government funds.

D. Indirect Costs and Transferred Cost.

These two areas, indirect costs and transferred costs, have been highlighted as a separate section of the audit program to emphasize that these areas have traditionally been vulnerable to unallowable costs.

1. The auditor should give attention to the vulnerability of indirect cost pools (such as general administrative expense pools and overhead pools) to unallowable costs.

a. Obtain a description of the accounts which comprise the general administrative and other indirect/overhead cost pools such as department overheads or administrative cost centers.

b. Based on account description, evaluate: i) whether any accounts appear inappropriate for the G&A or indirect cost pools in which they are included, or ii) whether any accounts appear vulnerable to being charged with unallowable cost.

c. Review costs in those indirect cost pools that appear vulnerable to being charged with unallowable costs.

2. The auditor should review costs transferred to the M&O's contract accounts from affiliates of the M&O such as the M&O's parent, home office, subsidiaries, and other divisions, sites, contracts, and facilities.

a. Determine if and how the M&O can transfer to its contract accounts costs from affiliates.

b. Obtain an understanding, document, assess, and test the internal controls to ensure that transferred costs are allowable and do not duplicate the types of costs that are covered by any contractual management allowance or fee arrangements.

E. Reconciling Costs Claimed.

1. In order to render an opinion on the allowability of cost, the auditor must ascertain the amount of costs the M&O claimed for the fiscal year(s) being audited. Obtain the amount claimed as allowable on the VANE. Also, obtain the supporting schedules and worksheets which detail cost by program and cost element.

2. Reconcile the costs claimed on the VANE to the M&O's general ledger and applicable subsidiary ledgers. Costs claimed in excess of amounts charged to the M&O's accounting records will be questioned as unallowable costs because they are unsupported.

3. Reconcile the costs claimed on the VANE to disbursements by the M&O

for the period being audited.

4. Reconcile the amounts claimed to the amounts DOE reimbursed the M&O through the letter of credit and/or other reimbursements.

5. Determine if amounts claimed in total and by program exceed contract ceilings and contractually binding program ceilings. Costs claimed in excess of contractual ceilings could be unallowable.

6. Review the year-end accrual process to determine if accruals were based on supported estimates and whether estimates appear to be significantly overstated or understated to compensate for a year-end funding excess or shortfall. Determine if any improper accruals impacted the allowability of costs claimed.

F. Transaction Testing.

The audit will test transactions to determine whether costs are allowable. This testing will follow appendix A of the audit program. The tests in appendix A should be adjusted to conform to the criteria for the M&O.

The auditor will decide on the amount of testing based on the results of the internal control assessment. In other words, the nature, amount, and extent of testing will be greater in those areas for which the auditor assessed a higher risk that the M&O could claim unallowable costs. However, the auditor should do some testing in every area, even if the risk in the area is minimal.

If risk in an area is assessed at maximum (i.e., the internal controls are non-existent or ineffective to prevent the M&O from claiming unallowable cost), the auditor needs to do extensive testing of transactions in order to reach a conclusion on the allowability of cost. Also, this internal control weakness should be reported.

The statistical sampling methods used should be sufficient to reach a conclusion on the costs and to project unallowable costs.

APPENDIX AALLOWABLE COST AT
MANAGEMENT AND OPERATING CONTRACTORSTRANSACTION TESTING

This appendix to the program describes transaction testing. It is based on general criteria that would normally apply to most management and operating contractors (M&O). The specific attributes will vary by contract and by the type of expense being tested. Therefore, the auditor should adjust the attributes to be tested based on the specific criteria applicable to the individual M&O.

For each item selected for testing, the auditor will test for applicable attributes. The attributes are listed numerically. Under each attribute are suggested steps (listed alpha-numerically) for testing for each attribute. The auditor should design specific steps based on the circumstances.

A. General:

1. Was the cost for an actual item received or service rendered?
 - a. The auditor should review supporting documentation and/or interview personnel to the extent necessary to conclude that the cost represents an item that the M&O actually received or effort which an employee, subcontractor, consultant, or vendor actually performed.
 - b. For equipment, physically observe the item and/or review relevant supporting documentation such as the receiving report and equipment inventory record.
 - c. For material, review relevant supporting documentation such as the receiving report, bill of material, logs, quality assurance report, or stockroom records.
 - d. For subcontractor, consultant, or vendor services, physically observe that the work was performed and/or review evidence such as time and effort reports, logs, time sheets, work orders, or time cards.
 - e. For a payroll cost, review time sheets, payroll, personnel, and other records to determine if an employee was a real employee who worked on the contract effort.
 - f. If sufficient documentation cannot be obtained to support a cost, interview M&O and DOE personnel to the extent necessary to conclude that the cost was allowable.
 - g. If the auditor cannot be satisfied that the cost was incurred, the cost is considered to be unsupported and therefore unallowable.

2. Is the cost supported by original documentation?
 - a. Review cost to determine if it is supported by original documentation such as properly completed and approved vendor invoices, receiving reports, time sheets, or other support.
 - b. Review cancelled checks or other evidence of payment (such as direct deposit evidence).
3. Is the cost properly classified by expense category?
 - a. Determine if the M&O identified and recorded the cost in the appropriate expense category. Proper expense categorization is essential to assess whether the M&O has identified and appropriately treated costs which the contract defines as unallowable costs or costs subject to certain ceiling and/or approval requirements.
 - b. Review cost details to identify if a portion of the expense should be separately categorized. For example, travel expenses might contain some unallowable entertainment expenses. Or, a vendor invoice might include some unallowable sales taxes.
4. Are the dollar amounts accurate?
 - a. Review all computations, extensions, allocations, and formulas to determine if the amount of the cost is accurate.
 - b. Determine if the vendor invoice rates agree with prices established in the purchase order.
 - c. Determine if subcontract charges were based on the subcontract's billing provisions.
 - d. Determine if travel costs were computed according to the contractor's reimbursement rates.
 - e. Determine if payroll costs were computed in accordance with the effort reported on the timesheet and the payrates identified in the personnel records.
5. Can the cost be traced to subsidiary and general ledgers?
 - a. Verify that the cost was properly recorded in the M&O's general ledger and any supporting subsidiary ledgers.
 - b. Verify that the cost was charged to the fiscal year in which it was incurred.
6. Was the cost included in the total amounts reported on the VANE, financial statements, and cost reports?
 - a. Verify that the cost was accurately included in the total

amounts reported on the VANE, financial statements, and cost reports.

- b. Verify that the cost was reported for the fiscal year in which it was incurred.
7. Is the cost's treatment consistent with other similar transactions?
- a. Based on the auditor's experience and observation of other transactions, evaluate whether the cost was treated consistent with similar costs. For example, evaluate if the cost was recorded against the same expense code as like costs.
8. Have prior OIG audits, internal audits, or appraisals at this M&O reported any findings or concerns relevant to this type of cost?
- a. Review copies of reports in OIG permanent files and discuss with M&O, internal auditors, and DOE representatives to determine if any prior reviews disclosed issues relevant to this type of cost.
 - b. Based on prior reviews, determine if any further audit steps are necessary in order to assess the allowability of the cost. For example, if a prior review identified fraudulent time sheets, the auditor might need to interview employees and supervisors rather than rely on the supporting timesheet. Or, if based on a prior audit, the contracting officer has ruled that a cost is unallowable under certain conditions, evaluate if this ruling has been complied with (see step G.1).

B. Reasonableness:

A determination of cost reasonableness often requires extensive review of the economy and efficiency of a function. Reasonableness is generally covered in performance audits. Therefore, the review for reasonableness in this audit could be limited to instances of cost that are obviously out-of-line as a charge to the contract. For example, an M&O would not be expected to charge personal food or clothing expenses. Similarly, an M&O would not be expected to charge home furnishings or amenities such as cut flowers. Likewise, in this step, we are not determining whether the M&O obtained the best possible price; rather, we are judging whether the cost appears significantly unreasonable for the item; e.g., the \$400 hamper, the \$100 meal, the \$100 per hour salary rate.

C. Applicability to the Contract (Allocability):

1. Is the item or service related to the contract effort?
 - a. Obtain a general understanding of the contract's scope of work.
 - b. Evaluate whether the item received or service rendered generally appears to be related to the contract effort. The purpose of this step is not to identify costs that can be avoided through management efficiency, although we should always be alert to leads in this area. Rather, the purpose of this step is identify unrelated costs. For example, an unclassified M&O would not be expected to incur the cost of a classified security container. Likewise, a solar energy M&O would not be expected to incur travel to a nuclear physics meeting. Be alert to costs that should have been charged to the M&O's other activities such as other contracts, other businesses (e.g., real estate subsidiaries), or auxiliary activities (e.g., student related activities in the case of a university).
2. Is the item or service related to the account to which it is charged?
 - a. Obtain a general understanding of the work scope for the budget and reporting (B&R) line, program, project, cost center, work order, or other unit identified with the account to which the cost was charged.
 - b. Evaluate whether the item received or the service rendered was related to the account to which it was charged.
3. Is the cost properly recorded as a direct or indirect cost?
 - a. Evaluate if the M&O properly characterized the cost as a direct or indirect cost. The criteria for this evaluation are: 1) the nature of the cost, and 2) the M&O's policy for distinguishing between direct and indirect costs.
 - b. Look for direct charges that the M&O improperly included in indirect cost in order to avoid program funding shortfalls.
 - c. Look for indirect costs that the M&O improperly charged directly to a program to avoid high indirect cost rates.
4. Does the cost duplicate the types of costs covered by a management allowance or fee arrangement.
 - a. If the contract provides for a management allowance or other fee arrangement, ascertain what types of expenses are covered by the arrangement.
 - b. Evaluate if the cost represents an expense covered by the management allowance or other fee arrangement.

D. Accounted for According to GAAP and CAS:**1. Is the cost accounted for in accordance with GAAP?**

- a. Compliance with GAAP is a requirement for allowability. Basic accounting issues such as cost identification, classification, timing, and reporting are covered by attributes tested in section A "General." There are not many other GAAP issues that impact on cost allowability. Accordingly, no additional steps are recommended. However, the auditor should be alert to GAAP requirements that could impact allowability of transactions such as leases, capitalized items, depreciation, and contingent liabilities.

2. Does the accounting treatment comply with applicable CAS?

- a. Compliance with CAS could be a requirement for allowability. The auditor should ascertain whether any CAS requirements are applicable to the contract. The auditor should test for compliance with any CAS requirements applicable to the cost being tested.
- b. Contracts generally require compliance with CAS 401 and 402. CAS 401 requires consistency in estimating, recording, and reporting costs, and CAS 402 requires consistency in distinguishing between direct and indirect costs. The attribute test in steps A.7.a and C.3 should satisfy these requirements.

E. Contract:**1. Does the contract identify the item or service as expressly unallowable?**

- a. Brief the contract to identify expressly unallowable cost provisions.
- b. The following is a list of costs generally defined as unallowable in contracts. It is intended to be a guide and not an all inclusive list. In some cases, a contract might permit charging these costs under certain situations. The auditor must follow the specific contract for criteria on allowable cost.

Advertising
Alcoholic beverages
Bad debts
Bonuses and similar compensation
Commissions, bonuses, and fees for obtaining
a contract
Contingency reserves
Contributions and donations
Dividends or other profit distributions
Excess depreciation
Entertainment

Facility capital cost of money
Fines, penalties, and late charges
First-class air travel
Insurance with contractor as beneficiary
Insurance on Government property
Interest
Legal expenses for proceeding brought by the
Government
Lobbying costs
Losses on disposition of contractor assets
Off-site offices
Organization expenses
Property furnished by the Government
Proposal preparation
Research and development outside the
contract's scope of work
Selling costs
Taxes

- c. Determine if the cost represents a cost which the contract defines as unallowable.
2. Does the cost comply with contract ceilings and limitations for this type of expense?
 - a. Brief the contract to identify cost ceilings and limitations. For example, a contract could have limitations on salary cost for employees earning over a certain amount or it could have ceilings on travel reimbursements such as the costs cannot exceed that permitted by Federal travel regulations. Also, contracts could have limitations on the amount that can be charged for employee morale, cafeteria deficits, safety shoes, special work-clothing allowances, and other employee related expenses.
 - b. Determine if the cost complies with applicable contract ceilings and limitations.
3. Have all prior approval requirements specified in the contract been met?
 - a. Brief the contract to identify specific prior approval requirements. For example, the M&O must generally obtain contracting officer approval prior to incurring such expenses as foreign travel, relocation, and overtime or prior to entering into subcontracts.
 - b. Determine if the M&O has obtained prior contracting officer approval if required for this cost.
4. If the cost is a payment to a subcontractor, has the M&O or the cognizant audit agency audited the cost or have appropriate arrangements been made for an audit?

- a. For a payment to a subcontractor under a cost-reimbursement subcontract, ascertain if the claimed cost has been audited by the M&O or the cognizant audit agency to determine allowability.
 - b. If the cost has not been audited, determine that payment is being made provisionally to ensure that the amount paid can be adjusted for the results of a future audit.
5. Is a contract compliance clause applicable to this cost; that is, if the contract clause is not complied with, the cost could be unallowable?
- a. For example, if the contract requires that material and supplies be obtained from government sources such as GSA and DOD, any excess cost resulting from purchases from non-GSA sources could be unallowable.
 - b. For a subcontract cost, did contractor comply with all contractual requirements for entering into the subcontract such as approvals and justification for sole source procurements.
 - c. Does the cost conform to requirements of any union agreements for which non-compliance could result in unallowable costs.

F. Laws and Regulations:

- 1. Does the cost violate any applicable laws that could effect the allowability of the cost?
 - a. Obtain a list of any laws that could have an impact on allowability of cost. If this list is in the auditor's permanent file, ensure that it is updated to cover the period being reviewed.
 - b. Evaluate compliance with any identified laws applicable to the cost that could impact allowability.
- 2. Does the cost violate any applicable regulations that could affect the allowability of the cost?
 - a. Obtain a list of any regulations such as DOE orders that could have an impact on allowability of cost. If this list is in the auditor's permanent file, ensure that it is updated to cover the period being reviewed.
 - b. Evaluate compliance with any identified regulations applicable to the cost that could impact allowability.

G. Contracting Officer:

- 1. Does the cost violate any contracting officer rulings, interpretations, or guidance which could impact the allowability of cost?

- a. From prior audits, permanent files, and discussions with the contracting officer, determine if the contracting officer has issued any rulings, interpretations, or guidance which could impact the allowability of cost.
- b. Evaluate compliance with any identified rulings, interpretations, or guidance applicable to the cost that could impact allowability.

SAMPLE AUDIT PROGRAM
FOR ALLOWABLE COST AUDIT

PHASE I

1. Issue the Announcement Letter. _____
2. Obtain and review the DOE prime contract and appendices and prepare a listing of (a) expressly unallowable costs, (b) costs with contractual limitations, which if exceeded, would be unallowable, (c) costs requiring DOE approval. _____
3. Conduct preliminary interviews to identify current internal control practices with regard to unallowable costs and the flow of transactions. _____
4. Perform sufficient transaction testing to support the understanding of the internal controls over unallowable costs obtained in the preceding step. _____
5. Prepare audit program upon completion and review with Audit Management. _____
6. Submit audit program to DOE and incorporate comments into program. _____

PHASE II

1. Review a statistical sample of Expense Reports and associated travel authorizations paid during the fiscal year to verify allowability in accordance with contract terms. _____
2. Review a statistical sample of accounts payable invoices for the fiscal year to verify cost allowability under all contract terms. _____
3. Review a statistical sample of employee personnel records to verify compliance with the Contract and proper authorizations associated with:
 - a. employee receiving pay over maximum salary range of the employee's grade range. _____
 - b. any individual whose annual compensation is at the level requiring DOE approval. _____
 - c. any other contractual limitations. _____
4. Determine if proper authorization for overtime hours and associated premium pay have been obtained from the Contracting Officer if required by the contract. _____
5. Determine if individuals receiving payment of extended sick leave for a longer period than their length of service warrants had documentation of required authorizations. _____

6. Review appropriate accounts and cost reports to determine if the following programs complied with contract guidelines:
 - a. recreation program. _____
 - b. reasonable cost of meals or refreshments for recognition of employees. _____
 - c. advertising. _____
 - d. exercise/wellness facility. _____
7. Review awards given to individuals to verify compliance with the contract and proper authorizations related to:
 - a. tangible savings. _____
 - b. intangible savings. _____
 - c. safety awards. _____
 - d. meritorious awards. _____
 - e. patent application awards. _____
 - f. patent issuance awards. _____
8. Determine if the Employee Service awards program is in compliance with the contract. _____
9. Determine if the Employee Recognition Program is in compliance with the Contract. _____
10. Review travel outside the Continental United States or any travel of more than 21 consecutive days for documentation of proper authorization. _____
11. Review documentation for the following types of cost to verify proper approvals and allowability:
 - a. advertising. _____
 - b. allowance for uncollectibles or bad debts written off. _____
 - c. home office costs allocated or billed. _____
 - d. corporate income tax. _____
 - e. professional services. _____
 - f. legal. _____
 - g. allowance for loss. _____

- h. donations. _____
 - i. general insurance and liability. _____
 - j. lease interest expense. _____
 - k. professional organization dues. _____
12. Perform sufficient test to insure compliance with contract terms not covered in the above steps regarding: i) expressly unallowable costs, ii) specific cost limitations, or iii) costs requiring DOE approval. _____

PHASE III

- 1. Reviews, index, and cross reference workpapers. _____
- 2. Submit workpapers for review. _____
- 3. Prepare summary of exceptions. _____
- 4. Prepare Draft Report. _____
- 5. Conduct summary meeting with appropriate management and incorporate management responses to detail comments section. _____
- 6. Issue Final Report. _____
- 7. Schedule follow-up review for corrective actions. _____

SUGGESTED AUDIT STEPS
FOR ASSESSING
INTERNAL CONTROL CHANGES

AUDIT STEPS

The following audit steps should be considered as part of the audit program for assessing internal control changes. They are not all inclusive. The OIG auditor should add other audit steps to assess internal control changes based upon his/her judgement about the condition of internal controls.

Internal Control System Changes

1. Determine if there were internal control deficiencies identified in audit reports issued by the OIG, GAO, internal auditors, or others during the past year. If so, list the deficiencies and determine if they led to internal control changes. Evaluate the changes made to the internal control system.
2. If audit reports were issued in the past year that contained internal control deficiencies and management did not take action to correct the deficiencies, determine if material weaknesses still exist.
3. Through discussions with field personnel, such as the Contracting Officer and Chief Financial Officer, determine if actions have occurred in the past year that may affect the internal controls of the M&O. If so, evaluate the actions to determine what changes have or should occur.
4. Based on the above steps, determine the risk that unallowable costs will be claimed by the contractor and paid by DOE.

Contract Terms

1. Verify that the M&O contract contains the audit clause required by the DEAR.
2. Review the M&O contract to determine if it has been materially changed in the past year and, if so, the significance of such changes to internal controls.
3. If audit reports issued throughout the year have identified conditions pertaining to contract terms, determine if such conditions have an affect on internal controls.
4. Based on the above steps, determine if there could be a risk that unallowable costs will be claimed by the contractor and paid by DOE.

Audit Reports by the OIG and Other Entities

Use the information from the above steps, as well as the fifth step in the assessment of the internal auditors' work.

A:AM22EXC.WPF

EXHIBIT C

Other Information Determined to be Relevant

Determine if our review identified material weaknesses that should be disclosed. If so, take appropriate action to disclose the material weaknesses.

SAMPLE ASSESSMENT PROGRAM
FOR OIG REVIEW OF INTERNAL
AUDITORS' WORK

In order to sign the annual VANE, the OIG must assess the work of internal audit staffs in order to verify that the internal auditors have met the contractual requirements with regard to allowable cost audits.

We should complete the following steps as a minimum to assure that we have performed an adequate assessment of the internal auditors' work:

1. Verify that the internal audit staff meets the GAO "yellow book" (page 3-15) criteria as to organizational independence, staff qualifications, and quality control systems.
2. Review the M&O prime contract and appendices and prepare a listing of unallowable costs. This list should also include costs with contractual limitations and costs requiring DOE approval.
3. Review the internal auditors' risk assessments with regard to the costs identified in step 2 above. This review of the risk assessment should encompass not only the inclusion of all potential unallowable costs in the risk assessment but, also, the reasonableness of the risk rankings developed by the internal auditors.
4. The M&O internal audit groups have the option of either performing a single annual audit for cost allowability or including steps with each audit program over a 5-year period to cover allowability of costs.

If the contractor chooses to perform a single audit for cost allowability, the cognizant OIG auditor should assess the internal auditors' report and workpapers using the criteria set forth in the GAO "yellow book" that describes the requirements for relying on the work of others. Give particular attention to the provisions of paragraphs 37b and 37d. The OIG auditor should conduct limited tests of the same audit universe to verify the accuracy of the conclusions made in the internal audit report.

If the internal auditors do not perform an annual audit for cost allowability but instead include a step in each audit to cover the allowability of costs, the cognizant OIG auditor may use judgment as to which internal audits he/she wishes to assess as well as the depth of such assessment. This judgment should be based on the perceived risk of unallowable costs being incurred in the area covered by the internal auditors. The "yellow book" criteria cited above should be used as guidance for assessing the selected internal auditors' work.

5. Review audit reports issued by the OIG and other entities (such as GAO, field office reviews, etc.) for possible impact in the area of cost allowability.

EXAMPLE OF REPORT ON ASSESSMENT OF INTERNAL CONTROL CHANGES
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITS
REGIONAL AUDIT OFFICE

Assessment of Internal Control Changes and Their Impact on the Allowability of Costs Claimed by and Reimbursed to XYZ Under DOE Contract No. DE-ACO-XXXXXXXXXX

Audit Report No. FR-VC-XX-XX

We have assessed the internal control changes by XYZ Company (XYZ) for fiscal year 19XX to assure that costs claimed by XYZ and reimbursed by the Department are allowable under the DOE contract.

Our assessment included an evaluation of the following:

1. Contract terms
2. Contractor internal control changes,
3. Audit reports by the OIG and other entities, and
4. Other information determined to be relevant.

DOE Order 2200.8B requires that the Office of Inspector General will periodically assess the reliability of the internal controls used by the contractor DOE to assure that only allowable costs are claimed and reimbursed. Each fiscal year the Office of Inspector General will sign the VA-NEA based on this assessment.

Because of inherent limitations in any control structure, unallowable costs may be incurred and not detected. Also, projection of any audit of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

BACKGROUND

XYZ's financial accounts are integrated with those of the Department, and the results of financial transactions are reported monthly according to a uniform set of accounts. Further, XYZ is required to account for all funds advanced by the Department, and to safeguard the Department's assets in its care.

The management of XYZ and DOE Field Office_____ are responsible for establishment and maintenance of an internal control structure including an internal audit that will ensure costs billed and reimbursed are allowable under the contract. According to contract terms, the contractor is required to annually conduct an internal audit of the records, operations, expenses

and transactions of the costs claimed to be allowable under the contract.

RESULTS OF ASSESSMENT

(Where no material weaknesses were disclosed)

In our opinion, changes to the internal control systems of XYZ for fiscal year 19XX provide reasonable, but not absolute assurance, that costs claimed by XYZ and reimbursed to the Department were allowable.

(Where material weaknesses were disclosed)

Our assessment disclosed conditions, including noncompliance with contract clauses and/or laws and regulations, in the internal control structure of XYZ in effect during fiscal year 19XX, which in our opinion result in more than a relatively low risk that unallowable costs will be claimed by and reimbursed to XYZ. Material deficiencies are shown in attachment 1.

RECOMMENDATIONS

(In the event there are no recommendations, a Department reply is not necessary. If there are recommendations, a reply is required and the report is subject to DOE Order 2320.2B which requires the formulation of an official Departmental position on IG reports.)

EXAMPLE OF REPORT ON ASSESSMENT OF INTERNAL AUDIT
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDITS
REGIONAL AUDIT OFFICE

Assessment of Management and Operating Contractor Internal Audit Function

Audit Report No. FR-A-XX-XX

AUDIT OBJECTIVES, SCOPE, AND METHODOLOGY

We have reviewed the internal audit function of XYZ Company (XYZ) at (date of last day of field work) to determine the extent to which the OIG may rely upon the work they have performed and thereby avoiding duplicative audit efforts. Our assessment was conducted in accordance with Government auditing standards and included the following tests:

1. Determining whether the auditors were qualified.
2. Determining whether the auditors were properly located in the organization in order to provide sufficient independence to conduct audit objectivity.
3. Determining whether the auditor's work was acceptable by examining, on a test basis, the documentary evidence of the work conducted.
4. Conducting tests of the work by examining similar transactions.

BACKGROUND

In October 1992, the Department initiated a tiered audit strategy for integrated and M&O contractors to improve communications and enhance the efficiency of existing audit resources. The implementation of the new audit strategy is expected to occur over the next several years and uses risk assessment methodologies as the basis for audit plans within the Department. This cooperative strategy incorporates the audit work performed by contractor internal audit staff (provided the audits comply with professional audit standards), Office of Inspector General (OIG), audits, and reviews conducted by operations offices. Specific internal audit requirements are identified in the DEAR clause 970.5204--9h and Acquisition Letter 90-3R.

RESULTS

(When no weaknesses were disclosed)

We found that the quality of work performed by the contractor internal audit function was sufficient to be relied upon. This assessment was based on our review of the internal auditors qualifications, independence, and audit workpapers, as well as conducting tests of the work by examination of some transactions, balances or work the internal auditors examined (or by examination of similar transactions, balances, or work, but not those actually examined by the internal auditors). Based on this review, no additional work would have to be done to accept the work of the internal auditors.

(When weaknesses were disclosed)

We found that the quality of work performed by the contractor internal audit function was inconsistent and was not always satisfactory. As a result, we conclude that overall the Department cannot rely on internal audit as an integral part of the Department's overall control structure. Based on this review, the following action(s) must be taken by the contractor at the direc-

tion of the operations office in order to accept the work of the internal auditors and are set forth as recommendations below.

RECOMMENDATIONS

(In event there are no recommendations, a Department reply is not necessary. If there are recommendations, a reply is required and the report is subject to DOE Order 2320.2B which requires the formulation of an official Departmental position on OIG reports.)

Inspector General Office of

cc: Director, Financial Audits (AO) Director, Audit Liaison (CFO)

Levels of Expression of Opinion on a VANEA

Opinion Level	VANEA Report ^{1/}	FMFIA Reporting
I. Unqualified	Signed	No mention
II. Qualified	Signed ^{2/}	Needed improvements
III. Disclaim	No signature ^{2/}	Material needed improvement(s)
IV. Adverse	No signature ^{2/}	Material needed improvement(s)

Explanation of Opinions

Unqualified - Indicates that based on sufficient audit review and testing controls are in place to assure that only allowable costs are charged to the contract.

Qualified - Audit has identified a non-material weakness and/or
- Audit scope has been qualified because of a lack of resources.

Disclaim - Existence of a material control weakness such as lack of internal audit clause or inadequate internal audit staff.

Adverse - Same as above, however, the effect is identifiable and measurable.

^{1/} The VANEA will be footnoted (at the OIG signature block), referring the reader to the OIG report accompanying the VANEA. The footnote will also indicate the type of opinion rendered in the report.

^{2/} These VANEA audit reports will contain a sentence mentioning that there are too few audit resources to fully carry-out what is envisioned in DOE orders and regulations. Thus, we are unable to assure that costs incurred are in all cases reasonable. However, if the M&O contractor has fully implemented the cooperative audit strategy, than there is no need to qualify the scope paragraph of the audit report.

(This exhibit not on disk.)
7-24-89

U.S. DEPARTMENT OF ENERGY
VOUCHER ACCOUNTING FOR NET EXPENDITURES ACCRUED

Exhibit H
DOE 2200.8A Chg 1
Attachment I-2

DOE F 2200.1
(05-89)
All Other Editions are Obsolete
Form Approved by
Comptroller General, U.S.

Public reporting burden for this collection of information is estimated to average 2 hours per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden, to U.S. Department of Energy, Office of Organization and Management Systems, Paperwork Reduction Project (1910-0600), 1000 Independence Ave., S.W., Room 4D-024, MA-813.2, Washington, DC 20585; and to the Office of Management and Budget, Paperwork Reduction Project (1800-0600), Washington, DC 20503.

OHS Control No.
1910-0600

CONTRACTOR _____ CONTRACT NO. _____
ADDRESS _____ FIELD ORGANIZATION _____
PERIOD: From _____, 19____ To _____, 19____

NET EXPENDITURES ACCRUED:

1. Net Cost of Operations After Special Items (From Statement of Operations) \$ _____
 2. Non-Reimbursable Transfers to and from Other Federal Agencies (From Cost-Budget) _____
 3. Reconciling Transfers to and from Other DOE Organizations (from Cost-Budget) _____
 4. Changes in Assets - Per Balance Sheet:
 - a. Accounts Receivable _____
 - b. Inventories _____
 - c. Plant and Equipment - Net _____
 - d. Prepayments _____
 - e. Collateral Funds and Other Deposits _____
- Net Expenditures Accrued \$ _____

I certify the above accounting was prepared in accordance with DOE reporting requirements, from records maintained in conformity with generally accepted accounting principles, and the net expenditures accrued have been incurred and in our opinion are allowable under the contract.

(Contractor)
By _____
Date _____ Title _____

DOE ADJUSTMENTS

	\$ _____

As Adjusted	\$ _____

Approved for the U.S. Department of Energy in the Amount of \$_____, subject to any adjustments disclosed by future audits.

Office of Inspector General (Date)

The above accounting conforms with generally accepted accounting principles, does not conflict with the provisions of the accounting directives, and accurately represents the accounting activity for the fiscal year. I hereby authorize this accounting to be reflected in DOE's accounts subject to any adjustments disclosed by future audits.

Head of Field Element or Delegated Procurement Official (Date)

Finance Director

(Date)

*Refer to OIG Report #_____. This report includes a _____ opinion.

22-H-1

I-17 (and I-18)

Release 3.0

CHAPTER 23PERFORMANCE AUDITS OF INTEGRATED CONTRACTORSA. SCOPE OF CHAPTER

This chapter sets forth general guidelines for conducting performance audits of integrated contractors. Performance audits include economy and efficiency audits and program audits.

B. ECONOMY AND EFFICIENCY AUDITS OF INTEGRATED CONTRACTOR FUNCTIONS

Functional activities are essential to the achievement of program objectives. The components of a contractor's organization and their related functional statements usually depict the functions which are conducted by the contractor in support of its principal programs. For most integrated contractors, a list of functions is formidable.

In most cases, functional responsibility is delineated according to organizational components. Individually and collectively, functional organizations provide (1) control and administration of resources and (2) the services required in direct support of program activities.

1. General Objectives of Economy and Efficiency Audits. The economy and efficiency audit program is designed to provide regular audit coverage of an integrated contractor's activities through examination of each function.

The general objectives of economy and efficiency audits are to determine the

- o extent to which agency resources are managed and used efficiently;
- o economy and effectiveness of functional practices in fulfilling assigned responsibilities;
- o reliability and integrity of management information reports on cost, schedule, and performance of functions;
- o extent of compliance with contract requirements and laws and regulations governing acquisition, management, and use of an entity's resources; and
- o adequacy of asset controls to provide reasonable safeguards against waste, loss, or misuse.

These objectives are general. Specific objectives need to be developed for each economy and efficiency audit to fulfill these general objectives. Chapter 24 lists specific objectives considered pertinent to each economy and efficiency audit. In developing an audit program, these objectives are to be augmented by other specific objectives developed from the results of the audit

survey. When a function is being audited by the OIG, additional objectives may be needed because the scope of the audit includes the Department's as well as the contractor's activities related to the audited function.

A brief discussion of each general audit objective follows.

a. Efficient Use of Resources - Cyclical audit coverage will include not only an examination of individual functional performance, but also an examination of the collective contribution of all applicable functions affecting the use of each type of resource such as cash, materials, facilities, equipment, and labor. Examination of the management and use of resources may cut across several functional organizations. The examiner must also consider (1) the resource status, and (2) the functions related to the planning, acquisition, control, and consumption of the resource. Functions are somewhat interdependent when considered from the standpoint of the event cycle affecting each type of resource. The audit guidance in chapter 24 provides for covering event cycles of each type of resource.

b. Economy and Efficiency of Functional Practices - Economy and effectiveness of functional services can be judged in several ways. Operating program management judges the effectiveness of functional support by the quality, timeliness, and utility of the services provided. Functional managers and higher echelon management are concerned with the cost as well as the effectiveness of functional services. If properly constructed, accountability reports should gauge efficiency and economy of functional operations, comparing costs and output to approved budgets and performance standards.

The auditor needs a thorough understanding of functional practices to be able to distinguish essential activities from supporting activities and unnecessary activities, and to suggest simplifying, combining, or eliminating activities.

c. Reliability and Integrity of Management Information on Cost, Schedule, and Performance - Cost and performance information is essential to good management. Reports should be constructed to meet the needs of management. Information in reports to management should be timely, complete, useful, and reliable. Each economy and efficiency audit should determine whether these criteria are being met. Additionally, it is important to ascertain whether the information in reports is being used effectively in the management and control of functional activities.

d. Compliance with Contract, Laws, and Regulations - Organizations are responsible for knowing what contract provisions and laws and regulations apply to their activities and for ensuring adherence to them. One objective of economy and efficiency audits is to determine the extent of compliance with these requirements.

e. Safeguarding of Assets - During economy and efficiency reviews, auditors would determine if the contractor is complying with requirements of laws and regulations that could significantly affect the acquisition, protection, and use of the contractor's resources. These audits provide an opportunity to examine asset safeguards in greater depth than do financial audits.

2. Correlation of General Audit Objectives with DOE's Internal Control Objectives. The preceding management objectives correlate to the objectives of economy and efficiency audits. Accordingly, each functional audit survey should include review and evaluation of reports and documentation relative to applicable internal control systems. This procedure provides valuable insight to the development of specific audit objectives.

3. General Audit Approach. The approach to an economy and efficiency audit of an integrated contractor involves

- o developing tentative audit objectives, using the guidance in chapter 24, and information concerning other areas known to interest management or the auditors;
- o performing an audit survey;
- o analyzing data accumulated during an audit survey;
- o developing an audit program, including refining the audit objectives and describing audit tests and other audit procedures;
- o examining and evaluating the function in detail and accumulating evidence in the form of workpapers; and
- o preparing and issuing an audit report.

Where an audit objective requires a determination regarding the adequacy or effectiveness of controls, the audit procedures in this Manual should include sufficient appropriate tests of transactions, balances, or other activities which are the object of the controls to make the necessary judgment or determination.

C. PROGRAM AUDITS OF INTEGRATED CONTRACTORS

Program audits may be undertaken at the request of management. They may also be scheduled based on information developed during economy and efficiency audits, particularly audits of labor, materials, and equipment. Likely, audits of resources will also develop information about the status of projects, which can be used in planning program audits. The reverse may also occur. Program audits may point to possible uneconomical or inefficient practices, which should be scheduled for review.

1. Planning and Scheduling Program Audits. No schedule or cycle is mandated for program reviews. However, the OIG has established a goal that at least one program audit should be performed during the 5-year audit cycle at each contractor location. This schedule will aid in establishing whether management practices and internal controls are effective in achieving the goals and objectives included in DOE-approved plans.

2. Program Ingredients at Any Level of Operation. Approved institutional plans, financial plans, and project order agreements covering work for others govern each integrated contractor's work. Assigned programs are divided into projects and tasks for accomplishment. Management of projects and tasks should (1) develop goals and objectives, (2) develop measurable criteria

to determine and evaluate progress, (3) establish target dates and milestones, and (4) establish a reporting system to apprise management of performance.

Results stemming from work conducted under established tasks or projects can be reviewed at any level where objectives and measurement criteria were established and where data to measure achievements exist. As used herein, the term "program audits" also encompasses audits of program subdivisions, such as projects and tasks, which are subject to measurement of results.

Without objectives and measurement criteria, a program review is not meaningful. However, it is possible to work with management to develop mutually acceptable objectives and measurement criteria, then undertake a program review based on the guidelines in succeeding sections.

The establishment of goals, objectives, and measurable criteria should be feasible for any aspect of work DOE contractors performed, except, perhaps, for basic research. However, even basic research projects should be based on detailed written plans and provide for technical evaluation of the documented results. The findings of such technical assessments should form the basis for judging the quality of research performed and for identifying new areas for future review.

3. Objectives of Program Audits. According to the Yellow Book, the general objectives of a program audit are to

- o assess whether the objectives of a proposed, new or ongoing program are proper, suitable, or relevant;
- o determine the extent to which a program or program subdivision has achieved the desired results;
- o assess the effectiveness of the program and/or of individual program components;
- o identify factors inhibiting satisfactory performance;
- o determine whether management has considered alternatives for carrying out the program that might yield desired results more effectively or at a lower cost;
- o determine whether the program complements, duplicates, overlaps, or conflicts with other related programs;
- o identify ways of making programs work better;
- o assess compliance with laws and regulations applicable to the program; and
- o assess the adequacy of management's system for measuring and reporting effectiveness.

Program audits also include a review of contract provisions, and DOE directives, as well as an evaluation of administrative controls which have a bearing on the attainment of specified goals and objectives.

4. Program Audit Procedures. As a minimum, the following procedures should be used to accomplish a typical program audit.

- o Conduct a preliminary survey of the program or project, or become familiar with the operations, verify its objectives, and identify the existing system for measuring effectiveness.
- o Use the guidance in chapter 6, as applicable, in conducting the preliminary survey. Additionally, review approved institutional plans, financial plans, and other program guidance.
- o Compare stated goals and objectives for each project or task over the past 3 years. When goals and objectives have been repeated each year, determine reasons for failure to achieve the objectives in the prior periods. This comparison may disclose that the goals are not sufficiently specific to measure annual progress, the goals were unrealistic, or resources were not applied according to approved plans.
- o Ascertain whether the current goals and objectives of the program or project are clearly stated in attainable terms and whether they are sufficiently specific to be measured against established criteria.
- o Determine whether the measurement criteria or performance indicators are valid and sufficient to enable measurement of results and accomplishments.
- o Ascertain, through appropriate tests, whether performance indicator data are accurate and reliable.
- o If complete and measurable criteria are absent, ascertain and evaluate the adequacy of the basis on which management at the reviewed level determines whether the stated goals and objectives are met.
- o Evaluate the adequacy of administrative controls which bear on the attainment of specified goals and objectives.
- o Based on the results of the preceding review, determine the extent to which the desired level of results or effectiveness was achieved. When results fall short of expectations, examine the underlying causes of ineffectiveness. Develop or estimate the cost of eliminating or reducing the influence of validated causes of ineffectiveness.

D. REPORTING

The guidance provided in chapters 9 and 10 covering audit reports can also be used in reporting on economy and efficiency and program audits of integrated contractors.

CHAPTER 24TYPICAL INTEGRATED AND M&O CONTRACTOR AUDIT AREAS**A. SCOPE OF CHAPTER**

This chapter presents implementing guidance relating to the OIG's audit strategy for M&O contractors. This chapter identifies typical contractor functions and suggests audit objectives for each function and subfunction. It serves as guidance to the OIG and M&O Internal Audit staffs. It's intent is to facilitate the planning, auditing and OIG tracking of audits performed at M&O contractors by the OIG, internal audit staffs, or contractually procured audit services.

B. AUDIT PLANNING AND RISK ASSESSMENTS

The OIG and M&O contractor audit plans should be based on risk assessment. Risk assessment by appropriate audit organizations will facilitate the best use of available audit resources. Audit plans based on acceptable risk assessment methodologies should provide adequate audit coverage over those areas most susceptible to waste, fraud and abuse. This risk assessment should include attributes such as adequacy of internal controls, length of time since last audit, dollar value/materiality, changes of systems, and results of prior audits. In addition, the audit organization utilizing this chapter should apply their own risk assessment which reflects their organization's unique needs, considerations, and requirements. The intent is to provide audit coverage over vulnerable areas on an annual basis. A more complete discussion of risk assessment is presented in Exhibit A of this chapter. Additionally, the OIG and internal audit staffs should document their risk assessment process and reasons for classifying functional areas as having low or no risk. The resulting audits should be performed in accordance with professional auditing standards. Compliance with professional audit standards will increase the OIG's reliance on the work of internal audit staffs. Specific internal audit requirements are identified by the DEAR 970.5204-9h and Acquisition Letter (AL) 90-3 as applicable to integrated and M&O contractors.

B. CONTRACTOR FUNCTIONS AND AUDIT OBJECTIVES

The chapter identifies contractor functions subject to OIG's audit. The following management areas represent the major integrated and M&O contractor functions.

Financial Management	Safeguards & Security Management
Procurement Management	Environment, Safety & Health Mgt.
Human Resource Management	Emergency Management
Construction & Facilities Mgt.	Government Property Management
Conservation Management	Quality Assurance Management
Data Processing Systems	Traffic, Fleet & Packaging Mgt.
Information Management	Planning & Budget Management
Support Services	

Typical functions and subfunctions and audit objectives are described in the following sections. This information is intended to help the OIG and internal audit staffs define the scope and objectives of each audit. Although audit objectives are provided for each function, the following general objectives are applicable to all functions.

- o Determine compliance with laws, regulations, and contract provisions that (a) govern the acquisition, management, and use of resources, or (b) have a material effect on financial information.
- o Determine whether audited functions are being managed efficiently and effectively, and within the terms of the DOE contract.
- o Determine whether programs, projects, and other activities are functioning as intended and are accomplishing their stated purpose or objective.
- o Determine whether internal controls are adequate, and will prevent, identify and report unallowable and unreasonable costs.
- o Determine whether allowable costs are addressed through either a single audit or as steps within other audits.

Although audits of programmatic activities can be performed at the contractor level, the audit coverage would be limited because program direction is at the Headquarters level (not the Field Office level) and such activities are usually carried out by more than one M&O contractor. Therefore, program areas have not been included in this chapter (See Chapter 23 for guidance on performance audits.).

A00 FINANCIAL MANAGEMENT

Financial management includes all activities related to the financial operations except for budgetary activities. Suggested audit objectives include determining whether:

- A00A o revenues and receipts are accurately recorded in accordance with requirements;
- A00B o assets, liabilities, rights and obligations of the entity;
- A00C o financial reporting conforms to the Department policies and procedures; and
- A00D o proper controls exist for all assets to safeguard against fraud, waste, abuse, unauthorized use, and misappropriation.

A01 Cash Management. This function encompasses all activities regarding the management and physical control of cash and negotiable items. Suggested audit objectives include determining whether:

- A01A o activities include internal controls which ensure prompt depositing of cash; proper control, accounting and processing of cash related

transactions; proper management of letters of credit and cash advance transactions; and credit card controls;

A01B o cash is safeguarded against waste, loss, unauthorized use and misappropriation;

A01C o adequate controls over imprest funds are in place;

A01D o cash balances are properly stated;

A01E o banking services are being received at lowest cost to the Government; and

A01F o cash balances etc., are at the minimum amount necessary.

A02 Accounts Payable. The function encompasses all activities regarding the management of accounts payable systems. The activity includes evaluation of financial accounting systems related to payments, including travel expenses and liquidation of contractually incurred liabilities. Suggested audit objectives include determining whether:

A02A o payments are made in accordance with contractual requirements;

A02B o internal controls exist to assure that timely, accurate, and proper payments are made;

A02C o disbursements are recorded and accounted for properly;

A02D o disbursements are made only for authorized expenditures; and

A02E o disbursements include control systems which ensure prompt payment.

A03 Accounts Receivable. This function includes all receivables associated with employee accounts, work for non-DOE entities, commercial accounts, and other miscellaneous receivables. Suggested audit objectives include determining whether:

A03A o the receivable balances are accurate and supported by subsidiary records;

A03B o all receivables are identified and recorded;

A03C o adequate internal controls exist for the aging, collecting, and write-offs of receivables; and

A03D o the recognition and handling of uncollectable accounts conform to contractual requirements.

A04 Property Accounting. This function includes the recording and classifying of all real and personal property in the accounting system. Suggested audit objectives include determining whether:

A04A o systems are in place to track the movement of property;

- A04B o periodic inventories are conducted and reconciliations performed between actual inventory levels and accounting system values;
- A04C o property classification and reporting conforms to DOE requirements; and
- A04D o "write-offs" of lost or damaged property conforms to DOE requirements and approved contractor policy.

A05 Reimbursable Accounting. This function includes evaluation of financial accounting systems associated with non-DOE funded work for others as addressed by DOE Order 2200.5B. Suggested audit objectives include determining whether:

- A05A o funding documents authorizing reimbursable work are compatible with work scope and provide funding consistent with DOE policy;
- A05B o direct and indirect costs are properly charged, to ensure full cost recovery;
- A05C o incurred costs accurately reflect work activity;
- A05D o work activity is within mission scope of DOE and acceptance of work meets DOE requirements; and
- A05E o work is not performed in advance of, or in excess of budgetary resources.

A06 Financial Accounting and Reporting, and Yearend Reviews. This activity includes the recording and classifying of all assets, liabilities, operating costs and equity in the accounting system, account reviews for unusual entries, applicable Cost Accounting Standards, compliance, and validations of balances. Suggested audit objectives include determining whether:

- A06A o all financial transactions are identified, classified and recorded properly;
- A06B o reliable financial reports are prepared;
- A06C o accountability of assets is maintained;
- A06D o the financial accounts are accurate and in accordance with approved accounting practices and contractual requirements;
- A06E o accruals during the fiscal year would significantly distort the validity of amounts shown on the VANE (see also Chapter 22);
- A06F o the reconciliation of all main financial accounting areas has been performed;
- A06G o financial reports are accurate and are supported by the detailed financial records; and

A06H o disclosure statement is complete, current and accurate, and has been approved by DOE.

A07 Payroll. This function includes all activities associated with the processing of time and attendance sheets and maintenance of pay and leave records. Suggested audit objectives include determining whether:

A07A o withholding and deductions are based on evidence of appropriate authorization;

A07B o compensation, gross pay, withholdings, deductions and net pay are correctly computed and are within contractual requirements;

A07C o payroll costs and related liabilities are correctly accumulated, classified and summarized in the accounts in the appropriate period;

A07D o controls exist to prevent duplicate payments, overpayments, and/or to fictitious employees; and

A07E o proper segregation of duties exist.

A08 Travel. This function relates to all types of authorized travel charged directly to a contract. Such travel should only be accomplished for essential purposes and at reasonable cost to the government. Suggested audit objectives include determining whether:

A08A o travel is properly authorized, i.e. domestic and foreign; and

A08B o travel costs charged to the contract are in accordance with contractual requirements.

A09 Cost Distribution System. This function includes the system used to develop, record and assign accurate costs to the final cost objective. Suggested audit objectives include determining whether:

A09A o costs are properly accumulated, distributed, and recorded;

A09B o internal controls exist to identify, prevent, and report unallowable and unreasonable costs;

A09C o the cost distribution base is in accordance with accepted accounting principles;

A09D o salary and labor costs (from payroll) are properly distributed to departmental accounts and job orders;

A09E o material costs, and other direct costs, are properly distributed;

A09F o overhead expenses are properly recorded and distributed to Departmental accounts, work orders and program classifications;

A09G o the proper production cost is allocated to product inventory cost; and

- A09H o the ending inventories are properly priced as required by applicable regulations and policies.

B00 PROCUREMENT MANAGEMENT

Procurement is guided by the rules, regulations, policies, procedures and limitations provided in the FAR, the DEAR, specific guidance issued by the Department, the terms of the negotiated contract, and the M&O contractor's DOE approved procurement system. For auditing purposes, procurement management is segregated into acquisition, receiving and inspection, and administration.

- B01 Acquisition. Contractor procurement actions should result in the most economical acquisition of supplies, services, and equipment and otherwise be in the best interests of the government. Suggested audit objectives include determining whether:

- B01A o the contractors procurement practices are in accordance with DOE policies;
- B01B o unusual features such as price escalation and price incentives were included;
- B01C o preaward cost and price analysis or audits required by the DEAR or FAR were conducted;
- B01D o acquisitions satisfy procurement objectives--e.g. verification of capability, price determination, and approvals; and
- B01E o consulting agreements, service contracts and contractual revisions are reasonable and consistent with programmatic requirements.

- B02 Receiving and Inspection. Goods and services provided by subcontractors and vendors should be properly authorized, received, accounted for, and controlled in accordance with established procedures. Suggested audit objectives include determining whether:

- B02A o the goods and services received were accounted for on a timely basis;
- B02B o only authorized goods and services are accepted and/or paid for;
- B02C o satisfactory physical controls exist over materials in receiving area;
- B02D o proper controls exist over rejected and/or reworked materials; and
- B02E o goods and services are inspected to determine conformance with specifications and other contractual conditions.

- B03 Administration. Each contractor's procurement administration should comply with requirements, regulations, and good business practice. Suggested audit objectives include determining whether:

- B03A o procurement modifications and change orders are justified, properly documented, and serve the economic interest of the Department of Energy;
- B03B o applicable DEAR and FAR procedures were followed;
- B03C o termination claims were audited and results were effectively used in claims settlement negotiations;
- B03D o proper procedures exist for the timely closeout of contracts; and
- B03E o subcontractor financial and technical performance is monitored.

C00 HUMAN RESOURCE MANAGEMENT

Human Resource Management focuses on whether actual practices and contractor policies governing Staffing, Education and Training, Compensation, Labor Relations and Benefits, Pension and Insurance Administration are in accordance with the contract provisions and applicable laws and regulations.

- C01 Staffing. Staffing includes activities associated with recruiting, classifying, reassigning and/or promoting employees as well as activities related to reviewing, approving and executing necessary disciplinary actions to maintain an effective work force. Suggested audit objectives include determining whether:
 - C01A o controls sufficiently ensure the recruiting, hiring, classifying and retaining of employees are consistent with programmatic requirements; and
 - C01B o appropriate DOE and corporate policies are followed in hiring M&O contractor employees;
- C02 Education and Training. Education and Training includes activities associated with employee development and those management activities associated with human resource development. Suggested audit objectives include determining whether:
 - C02A o an effective training program exists to provide for the design, acquisition, and delivery of quality training and organizational development experiences;
 - C02B o educational opportunities are consistent with DOE policies and contractual requirements; and
 - C02C o the training program requires courses needed to meet professional standards and other job related requirements as identified by law, DOE regulations or corporate policies.
- C03 Compensation and Salary Administration. Compensation includes activities directed towards assuring salaries are properly determined and positions are organized in the most efficient manner and related programs, such as, workers compensations, relations, salary scales, are

properly administered. Suggested audit objectives include determining whether:

- C03A o salary and wage structures are in accordance with the personnel policy described in the contract and applicable DOE policies;
 - C03B o job classification and promotion systems are administered equitably at all levels and in accordance with corporate policy;
 - C03C o employees are hired and retained only at authorized rates and benefits levels;
 - C03D o disciplinary mechanisms are in place to enforce corporate policies; and
 - C03E o termination policies are in place which are consistent with the contract and reflect DOE policies.
- C04 Labor Relations. Labor Relations includes activities of negotiating and making agreements with employee organizations on the rights, benefits and entitlements of employment. Suggested audit objectives include determining whether:
- C04A o the negotiating process resulted in an agreement that is mutually satisfactory to DOE, contractor and the labor organizations; and
 - C04B o independent cost estimates of the proposed agreement have been developed.
- C05 Benefits, Pension and Insurance Administration. This function includes management activities associated with employee benefit programs. Suggested audit objectives include determining whether:
- C05A o employee benefit programs have been approved by DOE and are efficiently, effectively and economically managed within contractual agreements; and
 - C05B o pension and insurance programs are administered and controlled in accordance with DOE policies, legal requirements and contract provisions.

D00 CONSTRUCTION AND FACILITIES MANAGEMENT

This function includes activities associated with facility planning, engineering, improvement, and management. It would also include activities related to the design and construction of new facilities or modification of existing facilities to perform DOE missions and programs. The major activities included are:

- D01 Site Development Planning. This includes all contractor activities related to developing, maintaining, and administering the DOE site development planning program. It includes activities such as the preparation of site development plans; reviewing site construction projects; space allocation; conformance with the approved site plan; and maintain-

ing an up-to-date site development plan library. Suggested audit objectives include determining whether:

- D01A o the overall activity ensures the efficient use of land, facilities, and utilities and also ensures that the priorities and scope of the planned construction activities meet the approved operational objectives; and
- o a system is in place to adjust site development plans to reflect changes in mission assignment.

D02 Construction Management. This includes primary activities such as preconstruction planning, architect-engineer (A-E) services, and construction project management. Other activities performed consist of administration of A-E and construction support contracts; reviewing project management plans; performing technical engineering and cost analyses, evaluating planning and construction methods; assuring compliance with design criteria; performing acceptance/operational tests in connection with final acceptance of the facility; and evaluating and making determinations regarding proposed change orders or contract modifications. All activities are performed to ensure that schedule, cost, construction methods and procurement plans are compatible with operational requirements, funding plans, criteria, scope of work, applicable DOE directives and Federal laws, and that construction activities are accomplished effectively and efficiently. Suggested audit objectives include determining whether:

- D02A o justification and approval exists for Titles I, II, and III engineering services;
- D02B o adequate competition for engineering services acquired externally existed;
- D02C o design errors were corrected at the least cost to the Government;
- D02D o construction completion schedules and milestones were adhered to;
- D02E o status reports to management were timely and accurate;
- D02F o construction progress is monitored by qualified personnel using approved techniques to track cost and schedule performance;
- D02G o design requirements were and are being met;
- D02H o in-process inspections were of adequate quality, at appropriate intervals, documented, and results reported to the proper individual(s); and
- D02I o final completion inspections were performed without undue delay and that construction errors were documented and corrected at minimal cost to the Government.

D04 Plant and Facilities Management. Facility maintenance activities assure proper maintenance of Government-owned, leased or controlled property. Suggested audit objectives include determining whether:

- D04A o the plant maintenance program is in accordance with DOE regulations and corporate policies and is adequate to prevent downtime, maintain health and safety standards, preserve Government-owned property, and best use maintenance resources;
- D04B o the capital asset replacement program is realistic, complete, and followed to assure economical operations;
- D04C o excess facilities have been identified to DOE; and
- D04D o a system is in place to identify maintenance projects requiring a Davis Bacon decision.

E00 CONSERVATION MANAGEMENT

Conservation Management includes the contractor's efforts, plans, programs, and projects designed to conserve resources of all kinds and to make significant improvements in the consumption efficiency of those resources. Suggested audit objectives include determining whether:

- E01 o conservation plans are in accordance with DOE policies, applicable laws and regulations and corporate policies;
- E02 o conservation goals were realistic and progress is measurable;
- E03 o conservation savings reports are timely and accurate; and
- E04 o the contractor has a viable program for conservation awareness and for soliciting conservation suggestions from employees.

F00 DATA PROCESSING SYSTEMS

This includes all activities related to the management and operation of multiprogram (general purpose) computer facilities, specifically equipment acquisition, maintenance and equipment utilization, software and systems development, applications systems, computer security, computer operations and administration, microcomputers and local area networks.

F01 Equipment Acquisition. The acquisition of EDP equipment begins with the initial planning process for a new or enhanced system or application or the replacement of existing equipment. Suggested audit objectives include determining whether:

- F01A o the equipment acquisition process considers all relevant factors;
- F01B o the resultant decision is cost effective, provides the needed capabilities, and fully supports operational objectives; and
- F01C o capital budgets and prioritization of needs are based on cost effectiveness, giving appropriate weight to replacement.

F02 Maintenance and Equipment Utilization. This function includes those specialized maintenance activities involving EDP equipment and the actual and projected rate of usage versus available capacity. Suggested audit objectives include determining whether:

F02A o there is a satisfactory system for reporting equipment utilization and downtime;

F02B o utilization reporting is accurate and complete;

F02C o management has acted effectively to reduce downtime;

F02D o inoperative and idle equipment is identified and repaired or disposed of;

F02E o there is a satisfactory system for reporting equipment malfunctions, repairs, and maintenance; and

F02F o the mix of in-house and vendor repairs and maintenance minimizes cost.

F03 Computer Security. This function includes all aspects of security associated with the computer hardware, such as: access controls, physical protection of the equipment, software security and data file access. The following audit objectives may apply and should be considered for other areas such as: Maintenance and Equipment Utilization, Computer Operations and Administration, Systems and Software Development, Applications Systems, Microcomputers and Local Area Networks. Suggested audit objectives include determining whether:

F03A o access to data files and programs is limited to those individuals authorized to process or maintain particular systems;

F03B o access to computer hardware is limited to authorized individuals;

F03C o the location, layout, and physical construction of the computer installation and the fire prevention, detection, and fighting techniques provide adequate physical protection;

F03D o there is adequate, regular, supervisory review of access and use activity and prompt review and investigation of violations and procedures for access and use;

F03E o controls are adequate to ensure processing and output are complete and accurate; and

F03F o controls provide reasonable assurance of continued operations in the event of damage or disaster, including backup, recovery and off-site storage procedures for programs and data.

F04 Computer Operations and Administration. This function includes the overall administrative management of the computer facility. Suggested audit objectives include determining whether:

- F04A o hardware errors are affecting the processing of transactions or the storing and accessing of data;
- F04B o the computer installation has a systems procedures manual which covers areas such as operations and security;
- F04C o there is compliance with recharge cost system requirements; and
- F04D o controls provide reasonable assurance that copyright laws covering proprietary commercial software are being observed.

F05 Systems and Software Development. This function includes those activities necessary to acquire and develop software. Suggested audit objectives include determining whether:

- F05A o the National Energy Software Center and other specialized computer software centers are researched for the availability of similar programs, or common-use portions of software programs, before software applications development is undertaken internally or purchased;
- F05B o internal software development has occurred only in instances when the software could not be acquired in a more economical manner;
- F05C o software development has followed the standards for vocabulary, programming, debugging, and documentation;
- F05D o implementation of systems have adequate application controls;
- F05E o development of systems meet management objectives or operate in accordance with original specifications;
- F05F o implementation of systems have been adequately tested; and
- F05G o implementation of systems that are susceptible to unauthorized modification have been identified.

F06 Application Systems. This function includes the design, testing, conversion and maintenance of new or modified applications. Suggested audit objectives include determining whether:

- F06A o input controls provide reasonable assurance that data received for processing by EDP has been properly authorized, converted into machine-readable form, and that data (including data transmitted over communication lines) has not been lost, suppressed, added, duplicated, or otherwise improperly changed;
- F06B o processing controls provide reasonable assurance that data processing has been performed as intended for the particular application, that all transactions are processed as authorized, that no authorized transactions are omitted, and that no unauthorized transactions are added;
- F06C o output controls reasonably ensure the accuracy of the processing result and receipt of the output by only authorized personnel;

- F06D o maintenance (updating and changing) of applications is adequately controlled and documented; and
- F06E o applications documentation, systems documentation, program documentation, and operations documentation are adequate to provide a sufficient understanding of these particular areas.
- F07 Microcomputers. This function includes the management of laptop, portable, and transportable computers. The audit objectives should consider whether these computers were acquired at reasonable cost, are utilized and controlled to a reasonable extent, and whether certain controls, such as adherence to copyright laws and backup of programs and files, are operational.
- F08 Local Area Networks. This function includes the management and administration of computer networks. In addition to the audit objectives listed for microcomputers, suggested objectives include determining whether:
- F08A o the network has an approved computer security plan;
- F08B o equipment was acquired in accordance with DOE regulations and corporate policies;
- F08C o the network design and implementation promote economy and efficiency of operations;
- F08D o network security provides access controls and protects software and data at levels defined by DOE regulations and corporate policies;
- F08E o software copyright laws and usage restrictions are adhered to; and
- F08F o backup and recovery procedures are provided at the level appropriate for the data processed or stored on the network.
- G00 INFORMATION MANAGEMENT
- G01 Telecommunications. This category includes activities associated with determination and installation of DOE's telecommunication requirements for data (records), voice (telephone), and radio/electronic communications. Audit objectives should focus on proper planning, adequacy and competency of management, appropriate budgeting, proper utilization, and use of good acquisition strategy. Due to the highly technical nature of this area, technical expertise outside the audit team may be necessary.
- G02 Records Management. This activity includes those activities related to records inventory, micrographics and protection of vital (classified and unclassified) records. The audit objectives are to determine whether records are maintained, used, and stored in an effective, efficient, and authorized manner and to determine compliance with records inventory and disposition schedules.

G03 Printing, Graphics, and Photography. This includes the activities associated with the internal production and/or acquisition of services and equipment for printing and publishing of technical and scientific reports, administrative documents, and forms; preparation of visual presentations such as viewgraphs, 35mm slides, supporting photography, and copying. Suggested audit objectives include determining whether:

G03A o printing, graphics, and photographic services are being obtained at least cost; and

G03B o the size of the printing, graphics, and photographic staffs is reasonable for the volume of output produced.

G04 Public Information. This includes those contractor activities associated with providing information to the public and the news media. Audit objectives are to determine whether the public information function is adequately staffed, appropriately managed, and properly protects the interests of the contractor and the Government when releasing essential information to concerned parties.

G05 Forms Management. This includes those activities which design, approve and monitor forms. Suggested audit objectives include determining whether:

G05A o Forms meet the following standards of design and use:

G05B o Forms conform with standards, guides, and principles set forth by GSA (as applicable);

G05C o Controls provide reasonable assurance that forms will employ standard equipment for writing, mailing, and filing, and minimize exceptions such as legal size forms; and

G05D o Standards and procedures exist for the approval and identification of forms.

H00 SAFEGUARDS AND SECURITY MANAGEMENT

This function includes all contractor activities associated with physical and technical security, international safeguards, personnel security clearance programs, and document classification. The audits should focus on evaluating the control systems for assuring adequate protection of nuclear weapons, materials, facilities, and transportation systems, controlling technology related to DOE's area of responsibility, and limited access to classified data only to cleared personnel with the need to know. The purpose of these audits would be to ensure that classified activities and information are safeguarded against loss or unauthorized use. The definitions and audit objectives for the major activities included under this function are as follows.

H01 Physical Security. This function includes all activities for ensuring protection of nuclear weapons, materials, and transportation systems against loss through sabotage, theft, or unauthorized use. It includes protective security or guards, whether provided by separate

contract, subcontract, or by the contractor's own employees. Suggested audit objectives include determining whether:

- H01A o the contractor has implemented and supports an employee security awareness program;
- H01B o special nuclear material, as defined in Atomic Energy Act of 1954, is adequately protected at all times as required by DOE regulations;
- H01C o the contractor's facility is covered by a security plan or program that ensures protection for employees and for Government owned assets against theft; and
- H01D o a mechanism exists for the prompt reporting to DOE of violations, infractions and other problems of a physical security nature.
- H02 Personnel Security. This function includes all activities for ensuring that access to classified information, facilities, and activities is limited to persons with a need to know and proper security clearances. Related activities such as "visitor control" and "reception" should also be included. Suggested audit objectives include determining whether:
 - H02A o the contractor has implemented and supports a viable personnel security program;
 - H02B o only the necessary employees possess security clearances;
 - H02C o facility access is permitted only to authorized individuals;
 - H02D o a reporting channel exists for communicating matters of personnel security concern to the appropriate DOE official; and
 - H02E o personnel security employee files are complete and current.
- H03 Document Classification and Declassification. The objective is to ensure that sensitive information developed in the Department's programs is identified, properly classified, and controlled as required by DOE regulations and corporate policies.
- H04 Technical Security. This activity is the Technical Surveillance Countermeasures (TSCM) Program. Departmental elements shall use all available means including physical security, technical surveillance countermeasures, personnel security, and communications security, including automatic data processing hardware and software security measures, to properly protect classified matter. Each DOE field office should have appointed a TSCM operations manager to manage the local program. Each integrated contractor should have appointed a TSCM officer. Suggested audit objectives include determining whether:
 - H04A o the contractor has appointed a TSCM officer;
 - H04B o the contractor and the specific TSCM officer maintain a technical surveillance countermeasures program that complies with the re-

quirements of DOE Order 5636.1A and local supplements to that order;
and

H04C o the TSCM program is operating effectively.

I00 ENVIRONMENT, SAFETY, AND HEALTH MANAGEMENT

This function includes all contractor activities associated environmental protection, safety, fire protection, health, hazardous waste management, and emergency preparedness programs. The audits consider control systems which (1) assure compliance with Federal, state, and local environmental protection, safety and health statutes, and related DOE orders and regulations; (2) protect against accidental loss or damage to DOE assets, (3) protect the well being of operating personnel and the general public, (4) analyze hazards, (5) assess and mitigate risks, and (6) collect, evaluate and disseminate accurate and reliable information regarding performance in these areas. The definitions and audit objectives for the major activities are described in the following sections.

I01 Compliance. The audit objective is to determine whether the program complies with Federal, state, and local environment protection, safety, and health statutes and related Departmental orders, policies, and regulations. In addressing this issue, auditors must be aware of environmental, health and safety requirements that DOE may have negotiated with the Environmental Protection Agency and state or local governments.

I02 Employee Safety and Health. In auditing employee safety and health, consider whether the occupational or industrial medical program:

I02A o ensures the health and safety of employees in their work environments through the application of occupational medical principles;
and

I02B o evaluates the physical and mental fitness of employees to perform job assignments without undue hazard to themselves, fellow employees, or the public at large.

I03 Hazard Analysis. In auditing hazard analysis, consider whether the analysis:

I03A o identified potential hazards;

I03B o analyzed potential consequences of identified hazards;

I03C o eliminated, controlled or mitigated the identified hazards; and

I03D o resulted in documented management authorization of the DOE operation based upon an objective assessment of the hazard analysis.

I04 Information Reporting. In auditing information reporting, consider whether the information reporting system provides for:

- I04A o investigation and evaluation of occurrences to their causes and the appropriate measures to prevent recurrences and improve the safety of DOE and DOE contractor operations;
- I04B o early, complete, and factual information on incidents or occurrences as a basis for (a) reports to the Secretary, Congress, and other Federal agencies, and (b) where appropriate, informing the public;
- I04C o adequate information on which to base management action;
- I04D o a basis for the improvement of codes, guides, and standards used in the DOE and DOE contractor operations;
- I04E o reporting of occupational radiation exposure information to the Radiation Records Repository; and
- I04F o monitoring, evaluating and reporting of onsite discharges, liquid and airborne effluents, and environmental conditions in the vicinity of DOE sites to assess the levels of radioactive and nonradioactive pollutants and their impact on the public and the environment.

J00 EMERGENCY MANAGEMENT

The audit objective is to consider whether the contractor has established and if required, tested their emergency response capability. Specific audit areas include determining whether:

- J00A o hazard assessments have been performed to identify potential operational emergencies;
- J00B o hazard assessment results were used to develop emergency planning and preparedness activities;
- J00C o the emergency management program incorporates the required 13 elements contained in DOE Order 5500.3A; and
- J00D o the contractor has established programs which incorporate DOE Order 5500.3A.

K00 GOVERNMENT PROPERTY MANAGEMENT

This function includes all activities associated with the management and control of DOE owned or leased property. The major activities and audit objectives are discussed in the following sections.

- K01 Real Property. The real property activity also includes activities associated with space management. Real property management activities include planning for future real estate needs; acquisition, control and disposition of DOE owned or leased real property; ensuring effective and efficient use of real property assets; and real property inventory management. Space management activities include planning for space needs; acquiring, controlling, and disposing of space; and ensuring for effective and efficient use of assigned space. The primary audit objectives would be to determine whether all real property is properly accounted for

in the appropriate inventory records and whether owned and/or leased space is used to the best advantage of the Government.

K02 Personal Property. This activity includes the development, implementation, and administration of policies, programs, and procedures for effective and economical acquisition planning, acquisition, receipt, inspection, storage, issue, use, control, protection, care and maintenance, disposal, and maintenance of operating records, (except accounting records) as appropriate, for Government personal property. This activity includes assets such as equipment, supplies consumed incident to the operation of the Department, equipment held for future uses. Suggested audit objectives include determining whether:

- K02A o the contractor is complying with the requirement for inventory of personal property, and, if so, whether the inventory records and balances are accurate and current; and
- K02B o the contractor is properly identifying, recording, and processing of all property including excess, scrap and surplus property.

K03 Materials. Materials held by the integrated contractor include, but are not necessarily limited to, stores, job stock, self service stock, precious metals, and nuclear materials.

A contractor's planning and control systems are usually interrelated with the functions of materials management. Decisions and actions relative to development of material requirements, acquisition of materials, administration of materials on hand, and consumption of materials in the course of fulfillment of a contractor's mission can all affect the relative cost of acquiring and carrying a materials inventory. Contractor management is responsible for finding the least costly combination of factors affecting materials costs commensurate with meeting mission requirements. Suggested audit objectives include determining whether:

- K03A o current use stores inventory reports are analyzed periodically for items to be deleted or for a reduction of stock levels;
- K03B o there is regular integrated planning between organizations requiring materials and those responsible for providing the materials;
- K03C o automatic stock replenishment procedures and practices are effective in satisfying demands and providing reasonable on-hand stock;
- K03D o warehouse facilities provide reasonable protection from the elements and theft;
- K03E o controls over precious metals have been implemented and that excess precious metals have been identified to the DOE precious metals pool manager under the DOE Field Office, Oak Ridge jurisdiction;
- K03F o materials are efficiently handled and physically protected and controlled during movement; and

- K03G o the integrated system of nuclear materials physical protection and material accountability and control measures effectively deters, prevents, detects and responds to thefts of nuclear materials.

K04 Sensitive Property. This activity includes the management and control of certain Government property items which are considered susceptible to being appropriated for personal use or which can be readily converted to cash as defined by DOE Order HQ 1400.1. Suggested audit objectives include determining whether:

- K04A o sensitive property has been identified by tagging and, if inventoried, is accurately shown on inventory records; and

- K04B o the extent of control is balanced by the cost to replace the lost item(s).

L00 QUALITY ASSURANCE MANAGEMENT

This function includes those composite activities at both the M&O contractors and their subcontractors to ensure that equipment and facilities perform satisfactorily when placed in service. A quality assurance program includes the policies and requirements for systems and techniques necessary to identify problems, implement corrective actions and monitor those actions to assure that implementation resolved the problems. Quality assurance applies to all aspects of research, development, engineering, procurement, construction and operations. Suggested audit objectives include determining whether:

- L00A o a quality assurance program have been developed and documented in accordance with specified requirements;

- L00B o objective evidence that documents the implementation of a quality assurance program;

- L00C o the quality assurance program is effective;

- L00D o the program identifies nonconformances and quality assurance program deficiencies; and

- L00E o corrections of identified quality assurance program deficiencies occurred.

M00 TRAFFIC FLEET AND PACKAGING MANAGEMENT

Traffic, fleet and packaging management is directed by the rules and regulations and policies established by the DOE and other applicable Federal, State and Local agencies and organization standards. The overall objective is to determine whether traffic, fleet and packaging activities and equipment are administered in accordance with applicable requirements and good business practices.

- M01 Fleet Management. This function includes activities to ensure effective and efficient planning, acquisition, maintenance, use, control,

and disposition of motor equipment, motor vehicles, aircraft, and watercraft. Suggested audit objectives include determining whether:

- M01A o acquisition is in accordance with predetermined long and shortrange plans;
- M01B o effective vehicles use is in accordance with GSA and other appropriate utilization measures;
- M01C o ultimate vehicle disposition nets the greatest return for the least usage cost;
- M01D o commercially rated passenger vehicles are operated within Department of Transportation (DOT) regulations;
- M01E o preventive maintenance programs are developed, implemented and carried out to assure effective, reliable fleet operation;
- M01F o fueling services are the most economical and meet requirements for continued fleet service; and
- M01G o controls, quality and economic considerations are exercised over the identifications, ordering and utilization of fleet parts, supplies and services.
- M02 Traffic Management. This function includes activities which assure the economical, efficient, effective, timely and safe shipment of hazardous material, hazardous waste, general commodities, household goods, and import and export items. Suggested audit objectives include determining whether:
 - M02A o services used are appropriate for the circumstances and transportation performance assessment is evaluated with consideration given to regulatory compliance, safety record and execution;
 - M02B o negotiated discounted tender rates are used properly and effectively;
 - M02C o the mode of transportation and carrier used is in the best interests of the government;
 - M02D o organizational internal assessments are adequately being conducted;
 - M02E o shipments are adequately described on bills of lading or other shipping documents;
 - M02F o insurance costs are avoided on shipments of Government-owned property;
 - M02G o the organization is complying with transportation requirements applicable to hazardous materials and hazardous wastes;
 - M02H o claims are being resolved equitably and within reasonable time limits; and

M02I o the organization is providing an adequate level of service to the organizations originating the shipments;

M03 Packaging. This function includes activities which assure the efficient, effective and safe utilization and implementation of DOE and DOT packaging and labeling requirements to assure the adequate control and delivery of hazardous materials, hazardous wastes and general commodities. Suggested audit objectives include determining whether:

M03A o the organization is complying with packaging regulations and requirements applicable to hazardous materials and hazardous wastes;

M03B o appropriate labeling is utilized to comply with hazardous material and hazardous waste regulation;

M03C o appropriate placarding is utilized to comply with transportation regulation and requirements;

M03D o maintenance programs are developed and implemented to assure safety and compliance with regulations and requirements for hazardous materials packaging; and

M03E o controls are in place and utilized identifying requirements for use of packaging.

N00 PLANNING AND BUDGET MANAGEMENT

Planning and budget management includes all activities associated with planning and budgeting, and funds control.

N01 Planning and Budgeting. This function includes financial programmatic, and strategic planning essential for the continued mission or for specific authorized contractual work. This function also represents the initial stage of the budget process in which requirements, budgetary assumptions and activity data are developed; estimates of funding requirements are prepared; detailed analysis and reviews are performed; budget data is consolidated and summarized; detailed justification are developed including prioritization of requirements; challenges are provided by internal and external reviewing and approving authorities; and budget changes are controlled and communicated throughout the organization. Suggested audit objectives include determining whether:

N01A o Formal Planning Process. Planning is formal, organized, and management supported, and the process considers all relevant sources of information and alternatives;

N01B o Budgetary Requirements. The budget process conforms to requirements, and provides a realistic portrayal of probable future events in conformity with department strategy, goals and objectives;

N01C o Budget Process. The budget process incorporates:
-- pertinent DOE requirements and limitations;

- detailed requirements of approved budgetary and program assumptions and approved program plans;
- appropriate workload measures of capability;
- estimates, when feasible, based on measures of workload, efficiency and effectiveness, and evaluated with techniques such as trend analysis;
- past results and alternative approaches to meeting objectives; and
- conformance to appropriate Cost Accounting Standards; and

N01D o there is a clear linkage with the contractual planning process, which in turn supports DOE strategic planning.

N02 Budget Execution. This function represents the budget process phase where fiscal year funding is provided to implement the Department's missions, functions, and programs. Audit work performed in other areas, such as finance and accounting, may be useful in an evaluation of budget execution. Suggested audit objectives include determining whether:

- N02A o there are appropriate systems, procedures, and reports capable of providing proper financial control as required by the contract;
- N02B o there are systems in place to monitor and analyze cost and schedule performance versus approved budgets and performance targets;
- N02C o there is an adequate work authorization and control process;
- N02D o general plant project funding limitations (\$1.2M) are exceeded; and
- N02E o capital projects are funded through use of expense funding, or split funding.

000 SUPPORT SERVICES

The functions of legal services, medical services, food services operations and custodial services are included in this section.

001 Legal Services. This function includes the contractor's organization to ensure compliance with all legal requirements, as well as the availability of legal assistance and opinions by employees and/or attorneys or legal firms on contract. Suggested audit objectives include determining whether:

- 001A o there is a time accountability system for the legal staff;
- 001B o the mix of in-house staff and outside law firms minimizes cost; and
- 001C o cost containment practices have been implemented, such as use of:

- mini-trials,
- mediation,
- arbitration,
- computer models to estimate the settlement value of a case at various stages of litigation,
- restrictions placed on the authority of outside law firms to subcontract for services, and
- consultants to audit invoices submitted by outside law firms.

O02 Medical Services. This function includes the medical facility, first aid station(s), or similar facility staffed by contractor's forces or provided by subcontractor. Suggested audit objectives include determining whether:

- O02A o medical services are provided at a reasonable cost for only medical care authorized under the contract;
- O02B o the contractor operated facility, as applicable, is properly staffed and managed;
- O02C o procedures ensure the early detection of illness by means of periodic health evaluations and treatment of work-related injuries according to the contract; and
- O02D o the service contributed to the maintenance of good employee health through the application of preventive medical measures, such as immunizations, alcohol and drug abuse programs, wellness programs, and counseling.

O03 Food Service Operations. This function encompasses those approved activities necessary for availing food products to contractor employees. This function includes vending machine operations. The function may be staffed by direct contractor employees or provided by subcontractor. Suggested audit objectives include determining whether:

- O03A o established financial objectives (break-even, based on full costs, including depreciation) are being achieved;
- O03B o food service is being provided economically;
- O03C o the food service facility is meeting the needs of the work force; and
- O03D o the concession for vending machines was competed in the past 3 years and whether controls exist to provide reasonable assurance that any commissions earned accurately reflect machine sales and are properly applied and administered in accordance with DOE agreements and the Randolph Sheppard Act.

- 004 Custodial Services. This function encompasses the routine and special housekeeping and cleaning duties by contractor-direct employees or as provided by subcontractor. The audit objective should be to determine whether custodial functions are performed economically and as scheduled.
- 005 Other Support Services. This function includes those support services not previously identified in this section. The typical audit objective would be to determine the economy, efficiency and effectiveness of the support services operations.
- X00 OTHER This function used for other miscellaneous items that do not fall within the other areas.

CHAPTER 25OFFICE ADMINISTRATIONA. SCOPE OF CHAPTER

This chapter establishes procedures for various administrative activities, including attendance procedures, office correspondence and communication, administrative or recurring reporting requirements, and billing other Government agencies for the OIG's audit services.

B. ATTENDANCE PROCEDURES

Policies and procedures for pay administration, hours of duty, time and attendance reporting, and leave administration are set forth in various DOE Orders and OIG Directives. To ensure uniform implementation of these policies within OA, the DAIGs and Regional Managers are responsible for ensuring that these policies and procedures are followed by OA personnel.

1. Hours of Duty. In accordance with OIG Directive IG-10A, "Pay Administration and Hours of Duty," issued 9-21-89, regular duty hours for full-time OIG employees are 8 a.m. to 4:30 p.m., with a 30-minute lunch break. Employees must complete an OIG form (see exhibit A, A:AM25EXA.WPF) when requesting hours other than 8 a.m. to 4:30 p.m. These forms will be submitted through channels to the AIGA for approval and should contain clear justification for approval of the deviation.

a. Deviations of more than 30 minutes from the standard work hours will be discouraged. Additionally, when persons are working on audits, they must adhere to the working hours of the office being audited. If staff meetings are scheduled in advance, all staff will be expected to abide by the hours established for each meeting.

b. Supervisors and Regional Managers shall review all requests for deviations in work hours and recommend approval or disapproval. If disapproved, the request will be returned to the employee along with reasons for disapproval. If approved, the request will be forwarded to the AIGA.

c. If the request is approved by the AIGA, the original document will be forwarded to the AIGP for certification and retention in the employee's Official Personnel Folder. Copies of the approved deviation will be furnished to the supervisor, the employee, and the office timekeeper.

d. A list of employees and their current duty hours will be posted at each work site (see exhibit B, A:AM25EXB.WPF). A copy of this list should be provided to AIGP when changes occur, such as employees adopting revised work hours or employees being added or deleted from the list.

2. Time Reporting. It is the joint responsibility of OA supervisors and employees to ensure that time and attendance is reported in accordance with all statutory and regulatory requirements. For management purposes, time charges should also be accurately reflected in the IGDBMS.

a. Time and Attendance Reporting - In accordance with DOE Order 3600.1B, "Time and Attendance Reporting," issued 2-11-91, all OA supervisors are responsible for keeping informed as to the attendance or absence of employees for whom they are responsible and ensuring the accuracy of time and attendance reports. Those individuals designated to certify time and attendance reports will be the supervisors most knowledgeable about and responsible for an employee's attendance.

b. IGDBMS Reporting - All employees shall be responsible for the input of their time into IGDBMS. The DAIGs and Regional Managers are responsible for ensuring that time charges entered into IGDBMS are consistent with that submitted on time and attendance reports. An optional form for recording work hours is provided in exhibit C.

3. Approving Overtime and Compensatory Time. Overtime work will be held to a minimum. It will be ordered or approved only when essential work cannot be accomplished during regular work hours by careful planning of work and scheduling of leave and other absence. Normally, all overtime work should be officially authorized and approved in writing and in advance. However, supervisors must keep in mind that employees who are covered by the Fair Labor Standards Act--i.e., nonexempt employees--are entitled to receive overtime pay if permitted to perform overtime work.

4. Leave Administration. The DAIGs and Regional Managers are responsible for establishing procedures within their office or region to ensure that leave granted meets legal and regulatory standards and is properly documented as annual, sick, or other leave, such as leave without pay, court leave, funeral leave, or administrative leave. They are responsible for scheduling annual leave with due regard for workload demands, the personal needs of employees, and the fact that leave lost at the end of the year can only be restored in cases where all legal and regulatory requirements are met, including timely written approval of the leave schedule or request. Supervisors are required to counsel employees who demonstrate a pattern of frequent sick leave usage of short duration. Additional guidance on leave administration is provided in DOE Order 3630.1B, "Leave Administration," issued 8-11-89.

5. Absence of Senior Staff. In addition to required time and attendance procedures, the DAIGs and Regional Managers will keep the AIGA informed of their absence from the office. This notification is required so that senior staff, or whomever has been delegated to act for them in their absence, can be contacted quickly and in an orderly manner.

a. Notification to AIGA - If a DAIG or Regional Manager is to be away from the office, he or she should notify the AIGA or the AIGA's Executive Assistant by telephone or E-Mail.

(1) Notification to the AIGA or the Executive Assistant should be made in accordance with the following requirements and timeframes:

- o Notification can be made on day of occurrence for unplanned sick leave and for annual leave and travel absences of one day or less.

- o Notification should be made two days in advance for absences of 2 to 4 days.
- o Notification should be made two weeks in advance for absences of one week or more in duration.

(2) The notification to the AIGA or the Executive Assistant should include the official's reason for being away from the office (annual leave, sick leave, official travel, etc.); inclusive dates of expected absence; name and phone number of person acting as DAIG or Regional Manager during the absence; and, when reasonable, telephone number where DAIG or Regional Manager can be reached during the absence.

(3) Prior approval by the AIGA is required for annual leave or travel absences of one week or more in duration. Approval is considered granted unless the DAIG or Regional Manager is notified otherwise within two working days after the AIGA or the Executive Assistant is notified.

b. Delegation of Authority - The DAIGs and Regional Managers are responsible for establishing procedures within their offices or regions for the delegation of authority whenever they, the ARMs, or Audit Directors are to be absent from the office for an extended period of time.

6. Reporting for Work During Hazardous Weather. Employees should report for work at their assigned offices or temporary duty locations unless, due to hazardous weather conditions, they are instructed otherwise. A hazardous weather condition--e.g., snow, ice, or floods--is one that may prevent employees in significant numbers from reporting to work, necessitate early dismissal from work, or the closing of Federal agencies in whole or in part.

a. For OA employees working in the Washington, D.C., area, information on closure of Federal offices or work-hour alterations due to hazardous weather is routinely provided to television and radio stations. However, employees must notify their timekeeper of an absence due to hazardous weather as soon as possible.

b. At other OA work sites, Regional Managers and Audit Directors are responsible for ensuring that employees are informed of procedures to be followed in case of hazardous weather. Normally, these sites will follow the policy established by the major DOE office at which the OA personnel are located.

C. OFFICE CORRESPONDENCE AND COMMUNICATION

Requirements for preparing correspondence and using Government communication services are contained in various DOE Orders and OIG Directives. Although most of these requirements are not repeated in this Manual, selected procedures for preparing correspondence and ensuring efficient use of Government communication services are provided below.

1. Preparing Correspondence. OA personnel should use DOE Order 1325.1A, "DOE Correspondence Manual," issued 6-18-81, as their basic reference for preparation of correspondence. In general, internal correspondence should be prepared on DOE memorandum paper, and DOE letterhead paper should

only be used for correspondence outside DOE. In addition, correspondence prepared for the signature of the IG or Associate IG--such as staff papers to DOE principals, memoranda to counterparts within DOE, and congressional correspondence--will be submitted to the AIGA for review and approval before being forwarded to the IG or Associate IG.

2. Signature Blocks. The use of standard signature blocks throughout OA provides the reader a better understanding of the writer's position. Individuals having organizational titles covered below are responsible for ensuring that the following signature blocks are used for all correspondence directed to addressees outside OA.

Signature Block	
OA Headquarters	OA Field Offices
(NAME) Assistant Inspector General for Audits	(NAME) _____, Manager Regional Audit Office Office of Inspector General
(NAME) Executive Assistant to the Assistant Inspector General for Audits	(NAME) Assistant Regional Manager Regional Audit Office Office of Inspector General
(NAME) Deputy Assistant Inspector General for Audit Operations	(NAME) _____, Director Audit Group Office of Inspector General
(NAME) Deputy Assistant Inspector General for Audit Policy, Plans and Programs	(NAME)* Auditor In Charge Audit Group Office of Inspector General
(NAME) Director for _____ Office of Inspector General	

*This signature block should only be used on correspondence dealing with a specific audit.

3. Keeping Telephone Listings Up-to-date - Employees should keep the AIGP telephone listing up-to-date. This listing includes telephone numbers, work locations, organization codes, and the preferred listing for sending an E-Mail message to an employee. Changes or updates should be called in to 6-4128 (for D.C. or Germantown employees) or to 202--586-4128 (for all other employees). Employees do not, however, need to inform AIGP of phone numbers at temporary duty locations.

4. Electronic Mail. OA staff are encouraged to use OA's E-Mail capabilities for sending messages and computer data files. In general, employees should ensure that E-Mail accounts listed in the AIGP telephone listing are checked at least once a day, and preferably 2 or 3 times a day.

5. Mail Service. In most instances, mail sent between DOE Headquarters and DOE field sites should be sent via field pouch service. The DOE Telephone Directory contains a listing of sites to which this service is available. This service is limited to material not exceeding 26 inches in girth. Additional guidance on mail service is provided below:

a. Use of U.S. Postal Service - All mail sent via the U.S. Postal Service to DOE organizations should be addressed in the following format:

Name and/or Title
Routing Symbol
Building Code
U.S. Department of Energy
City, State, Zip Code

b. Use of Express Mail - Requests for overnight air express service must be approved by office directors or other designated persons. A copy of the form to be used by DOE Headquarter's employees is illustrated in exhibit D (A:AM25EXD.WPF). Personnel at other locations should follow local procedures for approving use of express mail.

c. Mailing Workpapers - Frequently, workpapers need to be transferred between audit sites, regional offices, or Headquarters. When mailed, workpapers should be (1) carefully wrapped to ensure that packages or boxes are not likely to come open or be damaged in transit, and (2) sent via Certified Mail, with a return receipt requested.

D. ADMINISTRATIVE REPORTING REQUIREMENTS

In addition to its primary mission of conducting audits and reporting the results, OA is faced with other reporting requirements that occur on a regular basis. Substantial resources are often needed to fully respond to these requirements. Knowing when these events are going to occur and planning for their timely completion should increase the quality of finished products and reduce problems associated with last minute starts.

1. Weekly Activity Reports. Regional Managers are responsible for preparing weekly activity reports to the AIGA. The AIGA, in turn, prepares a weekly activity report to the IG. The activity reports should address such items as "current issues," "background/discussion," and "Blue/Buff Reports to be Issued." The DAIG/AO is responsible for coordinating OA's input to the IG.

2. Program Planning and Budgeting Requirements. Workload planning and budgeting requirements are discussed in detail in chapter 5. In general, AP³ is the lead office within OA for responding to these requirements, with substantial assist work provided by AO and the regional offices.

3. External Reporting Requirements. There are two major reporting requirements that occur within the OIG to which the AIGA has a substantial contribution--the OIG Semiannual Report to Congress and the PCIE Annual Progress Report to the President. These reports show the OIG's major accomplishments for each reporting period and are important in budget allocations since they are distributed to the Secretary of Energy, congressional offices, and the PCIE. Because of the broad uses of these reports, it is

important that OA have adequate procedures to ensure the development of consistent and accurate data.

a. Point of Contact - In accordance with OIG Directive IG-206A, "Office of Inspector General Semi-Annual Reports," dated 2-10-89, the DAIG/AP³ will be OA's point of contact for providing AIGP with requested highlights of OA activities, summaries of major reports, and other data in accordance with milestones established by AIGP.

b. Reporting Timeframes - The submission of Fact Sheets is an ongoing process, and other reporting requirements will be adjusted according to specific data calls by AIGP. The input for Semiannual Report must be submitted in a timely manner so that the AIGA can complete work by April 20 and October 20. The input for the PCIE Summary Report must be submitted in a timely manner so that the AIGA can complete work by October 20. Input must be submitted in a timely manner in order to meet prescribed due dates.

c. Preparation of Fact Sheets - As audits are completed, Regional Managers are responsible for ensuring that auditors prepare Fact Sheets as part of the final report package and submit them to AO for review. Instructions for preparing the Fact Sheets are provided in chapter 11, exhibit H (A:AM11EXH.WPF). Auditors should ensure that the narrative in the Fact Sheets accurately summarizes the monetary or programmatic impact of the audit since this narrative provides the source material for preparing the semiannual reports. Report numbers should be provided with each narrative.

(1) Blue Cover Reports. A narrative suitable for inclusion in the semiannual report will be provided at the time the report is presented to the IG for signature.

(2) Buff Cover Reports. Narratives applicable to Buff cover reports will be submitted within 15 days of the publication date.

(3) All Other Reports. Narratives of other audit reports considered of sufficient significance to warrant highlighting in the semiannual report will also be submitted within 15 days after publication.

d. Semiannual Audit Report Writeups - In general, the semiannual reports are prepared by the IG and AIGP using the Fact Sheets and the Monetary Impact Reports submitted by the regional offices. AO is responsible for ensuring that audit results for all audit reports are available to the IG for preparing the semiannual reports and that the information selected by the IG for inclusion in the semiannual reports is accurate and reflects the audit's current status and impact.

e. Monetary Impact of Audits - AP³ is responsible for coordinating with the Office of Compliance and Audit Liaison in the Office of the Chief Financial Officer to determine management actions and monetary impact of all IG issued audit reports. Generally, differences between management and OA auditors in the estimated monetary impact of an audit should be resolved during the audit reporting process. Should differences still exist after a report is issued, AO will be responsible for meeting with Audit Liaison staff on an as needed basis to resolve such differences.

f. Statistical Data - AP³ is responsible for ensuring that statistical data to be incorporated into the semiannual reports is provided to AIGP by April 15 and October 15 of each year.

4. Other Recurring Requirements. Although requirements for performance appraisals, financial disclosure statements, and awards are discussed elsewhere in this Manual, general timeframes for these recurring requirements are provided in exhibit E.

E. BILLING OTHER GOVERNMENT AGENCIES FOR DOE/OIG AUDIT SERVICES

It is AIGA policy to be as responsive as possible to the program officials of other Government agencies requesting audit services of the AIGA. The OIG currently serves as "cognizant auditor" for auditing various contractors nationwide. As cognizant auditor, the OIG does routine reimbursable contract audits (preaward, overhead rates, cost-incurred, closeouts, etc.) in support of contracting officers at other Federal agencies. Under this concept, one Federal agency audits a particular contractor for all other Federal agencies, such as required by OMB Circular A-73. It is the responsibility of AP³ to assure that OA has reimbursable agreements with the agencies for whom it serves as cognizant auditor.

The Regional Managers are to gather and process the information needed to bill other agencies for reimbursable audit work. This information will be submitted to the DAIG/AP³. The approved documentation will be forwarded to AIGP which has responsibility for processing it through DOE's accounting channels. The charges for OA's auditing services will be based on applicable established hourly rates plus travel and other expenses. Where audit services are contracted out, the charges should include any OA costs plus the full cost paid to the contractor.

REQUEST FOR CHANGE OF DUTY HOURS

To: _____
(Supervisor)

I, _____, request that my official
working hours, Monday-Friday, be changed as follows: From

_____ to _____, for the

following reason(s): _____

(Date)

(Signature)

Supervisor: _____
(Signature)

() I recommend approval.

() I disapprove. My reasons are given
below.

(Date)

Second Level Supervisor: _____

(Signature)

(Date)

() I concur.

() I do not concur.

Assistant Inspector General
for Audits

(Date)

Assistant Inspector General
for Policy, Planning and
Management

(Date)

cc: Supervisor
Timekeeper
Personnel Officer
Chief Timekeeper
Employee

APPROVED WORK HOURS FOR (THE OFFICE OF . . .)

AS OF _____

	<u>FROM</u>	<u>TO</u>
Auditor, Able	8:00	4:30
<u>Bee, Queen</u>	<u>8:15</u>	<u>4:45</u>
Bullet, Fast Asa	8:00	4:30
Charge, Whosein	8:00	4:30
<u>Cover, Buff</u>	<u>7:30</u>	<u>4:00</u>
<u>Delegate, Over</u>	<u>8:30</u>	<u>5:00</u>
Error, A. Gross	8:00	4:30
Folk, Comm'n	8:00	4:30
Good, Better B.	8:00	4:30
<u>Hunt, Witch</u>	<u>7:30</u>	<u>4:00</u>
Index, Cross X.	8:00	4:30
Junkie, Detail	8:00	4:30
<u>Kontract, Miss Spell</u>	<u>7:30</u>	<u>4:00</u>
<u>Labor, Manual</u>	<u>8:30</u>	<u>5:00</u>
Mark, Tick	8:00	4:30
Newperson, Susie Q.	8:00	4:30
Overrun, Days	8:00	4:30
<u>Priority, High R.</u>	<u>7:45</u>	<u>4:15</u>
Quick, Pretty D.	8:00	4:30
Rewrite, Dudley	8:00	4:30
<u>Sample, Random</u>	<u>7:30</u>	<u>4:00</u>
Stickler, B. A.	8:00	4:30
Training, Onjob	8:00	4:30
<u>Wheels, Spin</u>	<u>8:15</u>	<u>4:45</u>

NOTE:

Except for the standard work hour deviations noted (see underscoring), all persons are expected to abide by the normal work hours of 8 a.m. to 4:30 p.m. Further deviations to this schedule are not authorized without advance approval from the AIGA, in accordance with OIG Directive IG-10A.

Date: _____

Reply to
Attn of: _____

Subject: Request for Overnight Air Express Services

To: Chief of Logistic Operations Branch, MA-235.2

Request the following items be sent by Overnight Air Express:

Letter Contents 1. _____
2. _____
3. _____
Package Contents 1. _____
2. _____

Sent to: Name: _____
Address: _____
City: _____ State _____ Zip _____
Phone: _____
(No P.O. Box accepted)

Justification: _____

It is absolutely essential that the above items be delivered by:

DATE _____ TIME _____

An inquiry has been made at the DOE Mail Facility, delivery of this item (or items) cannot be accomplished by the U.S. Postal Service next day Air Express. DOE Mail Supervisor that gave the above information:

NAME _____ TITLE _____

Signature _____
Type Name _____
Title _____

[THE APPROVING OFFICIAL MUST BE THE ADMIN. OFFICER OR DIVISION DIR.]

CHAPTER 26PERSONNEL MANAGEMENT**A. SCOPE OF CHAPTER**

This chapter summarizes DOE and OIG personnel management procedures as they apply to OA.

B. GENERAL PERSONNEL POLICIES

General policies for personnel administration, work force discipline, and various employment policies are discussed at length in various DOE Orders and OIG Directives. Requirements of particular relevance to OA managers, supervisors and employees are summarized below.

1. Personnel Administration. OIG Directive IG-26, "Administration of General Personnel Authorities," issued 11-7-89, establishes policy and guidelines for OIG personnel management responsibilities. In accordance with this Directive, OA supervisors and managers shall:

- o Define job duties, select employees, and assign work and responsibilities;
- o Develop and motivate employees, and evaluate employees' performance, integrating performance objectives with organizational goals and the OIG mission;
- o Take appropriate action to recognize superior performance and to correct deficiencies noted;
- o Deal with all employees and employee representatives in a fair and equitable manner and in accordance with established policy, including terms of negotiated agreements;
- o Apprise employees of their role in accomplishing the OIG mission, and of their rights, privileges, and obligations as Federal Government employees; and
- o Keep employees informed of policy and management decisions affecting their employment and mission accomplishment.

2. Access to Personnel Records. Personnel records are accessed by employees, designated representatives, managers and the public on a need-to-know basis. OA employees generally may obtain access to files related to them and their official positions by requesting such access directly from the OIG personnel office. The employee may be accompanied by a representative or may designate one in writing who is authorized to review specific records pertaining to the employee. Managers generally may obtain access to files related to the employees they supervise through the OIG personnel specialist.

AIM

Association for Information and Image Management

1100 Wayne Avenue, Suite 1100
Silver Spring, Maryland 20910
301/587-8202

Centimeter

Inches

MANUFACTURED TO AIM STANDARDS
BY APPLIED IMAGE, INC.

7 of 7

3. Work Force Discipline. OIG Directive IG-22, "Work Force Discipline," issued 7-24-89, provides guidance and procedures, and states responsibilities for maintaining work force discipline in the OIG. In accordance with this Directive, OA supervisors and managers shall:

- o Keep employees informed of rules, regulations, and standards of conduct, and maintain order and discipline within the framework of established procedures;
- o Gather, analyze, and consider carefully all facts and circumstances before taking or recommending corrective action; and
- o Issue oral admonishments, notices of reprimand, and initiate proposed actions after consultation with the Personnel Officer.

C. RECRUITMENT AND PROMOTIONS

Various DOE Orders and OIG Directives provide detailed procedures for recruiting new employees, setting rates of pay for both new and current employees, establishing within-grade increases, evaluating and selecting candidates for promotions, and evaluating the performance of managers and supervisors during a probationary period.

1. Recruitment. In accordance with OIG Directive IG-28, "Merit Promotion," issued 11-7-89, OA supervisors and managers will fill vacant positions from the best available candidates and in accordance with Federal policy and applicable civil service laws and regulations. In particular, OA supervisors and managers will ensure that policies on affirmative action and upward mobility are followed.

a. Affirmative Action - All OA supervisors and managers are responsible for (1) ensuring that they and their staffs actively participate in the search for minorities, females, handicapped individuals and disabled veterans in the recruitment of personnel; (2) evaluating vacancies in light of their adaptability to the Upward Mobility Program; (3) identifying trainee and target positions when such action is consistent with OA's needs; and (4) systematically developing lower graded employees whose current assignments do not provide for any further advancement.

b. Upward Mobility - All OA supervisors and managers will ensure that underrepresented minorities and women are provided the opportunity to compete for assignments to trainee positions which will enable them to progress to administrative, professional and technical positions within the office.

2. Within-Grade and Merit Increases. OA supervisors and managers are responsible for applying the provisions of DOE Order 3540.1A, "Performance Management and Recognition System" (PMRS), issued 8-14-86, and OIG Directive IG-10A as they pertain to merit and within-grade step increases. Specific responsibilities include certifying that subordinate employees have performed at an acceptable level of competence for merit or within-grade increases, or preparing recommendations for the withholding of within grade increases. Supervisors should consult AIGP's Human Resources Management Division when an employee's performance is such that zero merit increase or denial of a

within-grade increase is contemplated.

3. Promotions. Promotions at all grade levels are to be supported by a documented performance record that equals or exceeds the candidate's current performance requirements, and gives indication that the candidate being considered will equal or exceed the performance requirements of the position for which the candidate is being considered. For candidates in professional job series, such as auditors, the ability to develop an acceptable written product is essential to career progression. The candidate's demonstrated integrity in work habits and audit products, and loyalty to the goals, mission, and policies of the OIG and OA are also important factors to be considered before promotions are recommended.

a. OIG Directive IG-28 provides detailed procedures for the OIG Merit Promotion Plan. In general, this Directive applies to all General Schedule (GS) and merit pay positions in grades 1 through 15, as well as various actions involving greater promotion potential than permanent positions currently held by employees.

b. Promotions to grades 13, 14 and 15, as well as selection for training which is required in order for an employee to be promoted to these grades are also subject to actions by the Audit Career Advisory Panel (ACAP), as discussed in section G of this chapter.

4. Probationary Period for Managers and Supervisors. OA's success in carrying out its mission is dependent to a large extent on the caliber of its managers and supervisors. Incumbents of these positions must demonstrate effective managerial and supervisory skills and abilities which cannot be readily taught or developed in other kinds of positions. In order to assess a new appointee's supervisory or managerial ability, a 1-year period of probation is required of all newly appointed managers and supervisors. In the event that perceived potential to perform as a manager or supervisor does not result in acceptable performance of those duties during the period of probation, a newly appointed manager or supervisor shall be removed from the supervisory or managerial position and shall be assigned in accordance with the provisions of OIG Directive IG-23, "Probationary Period for Managers and Supervisors," issued 9-21-89.

D. RELOCATION AND REASSIGNMENT

Teamwork and knowledge of operations are important to an effective organization. One way to improve both is to permit staff members at all levels to learn as much about the jobs of others as possible. Although considerable knowledge can be gained through periodic meetings and discussions, that is not the same as knowledge gained by experiencing the work that others are required and expected to do. The DAIGs and Regional Managers are encouraged to explore staffing options that broaden the knowledge and understanding that staff members have of OIG and DOE operations at various locations.

1. Permanent Relocation. Employees in one office or region may request permanent reassignment to another office or region. Such assignments would involve a Permanent Change of Station and are subject to AIGA approval.

2. Temporary Assignments. With AIGA approval, the DAIGs or Regional Managers may request that an employee be detailed on a temporary basis to fill a position at another location. Likewise, employees in one office or region may request assignment to another office or region on a temporary basis. Such assignments would normally be for 120 days or less and would not involve a Permanent Change of Station. A temporary reassignment of this nature could be particularly opportune when an organization has a position vacancy due to promotion or retirement, and the replacement is not due to arrive for a period of time. When an employee is temporarily promoted, reassigned, or detailed for more than 120 calendar days, a separate performance appraisal must be obtained for consideration by the rater who prepares the employee's annual performance appraisal.

E. PERFORMANCE APPRAISAL PLANS

Responsibilities and procedures for an OIG performance evaluation and rating plan are provided in OIG Directive IG-36B, "Performance Appraisal Plans," issued 10-19-90. In accordance with this Directive, OA's supervisors and managers are responsible for ensuring the accuracy of each employee's position description, identifying job elements (including critical elements) of the position, setting the standards of performance, and evaluating each employee against established standards annually. Interim evaluations are also required by the AIGA.

1. Setting Performance Standards. Standards are set in accordance with the procedures described in DOE Order 3430.3A, "Departmental Performance Appraisal System," dated 8-14-86, and must be finalized and in place before the appraisal period can begin. Establishing standards properly, and in a timely manner, is an important part of every supervisor's function. Failure to do so must be addressed in evaluating the supervisor's own performance.

2. Appraisal Periods. Appraisal periods are provided in the following table:

<u>Type of Employee</u>	<u>Appraisal Period</u>		
	<u>Begin</u>	<u>Following Year</u>	
		<u>Interim</u>	<u>End</u>
General Schedule employees	June 1	Dec. 1	May 31
Merit Pay employees	July 1	Jan. 1	June 30
Senior Executive Service	Aug. 1	Feb. 1	July 31

3. Assigning Performance Ratings. The DAIGs and Regional Managers are responsible for ensuring that employee performance ratings are assigned in accordance with the procedures described in DOE Order 3430.3A and the following timeframes.

- o A rating official (normally an employee's immediate supervisor) is responsible for completing the official appraisal form, signing it, and forwarding it to the reviewing official (usually the employee's second-line supervisor) within 7 days of the end of the rating period.

- o The reviewing official completes the review and signs the appraisal form within 14 calendar days of the end of the rating period.
- o The rating must be discussed with the employee and the employee's signature obtained within 21 calendar days of the end of the rating period.

F. STAFF RECOGNITION

All forms of recognition are to be based on solid achievements by the person being honored. The form of recognition may range from a promotion to a simple "Thank You" (letter of commendation) for a job well done.

1. Responsibilities. The DAIGs and Regional Managers are responsible for initiating all actions designed to recognize OA staff members who have contributed to OA's mission in a substantial way.

2. Quality Step Increases. Quality step increases may be granted only to GS employees who have permanent or indefinite appointments, whose current rate of pay is less than the maximum for their grade, whose current rating of record is "outstanding," and who are expected to continue to serve in their current position, or in a similar position at the same grade, and at the same level of performance, for at least 60 days. Guidance for these increases is provided in OIG Directive IG-10A.

3. Incentive Awards. Both GS and merit pay employees are eligible for incentive awards, both monetary and nonmonetary, in accordance with the provisions of DOE Order 3450.1B, "Incentive Awards," issued 6-23-92. Incentive awards are an appropriate form of recognition in cases such as:

- o In special work situations of limited duration or where achievements are otherwise nonrecurring;
- o In recognition of group achievement;
- o When an employee's level of performance of regular duties merits some form of cash recognition, but his or her length of service in the position is insufficient to clearly indicate that such performance is typical of the employee and, therefore, likely to continue; or
- o Where the conditions for a quality increase are met, but the employee would enjoy the benefits of an additional step increase for an insufficient length of time, such as when nearing retirement.

4. Annual Awards. For purposes of recognizing sustained, quality audit work, the following annual awards are established and are to be integrated into the existing award/bonus structure.

- o Annual Assistant Inspector General Award. To be awarded annually to the person in grade GS/GM-14 and below who contributes the most during the year to OA's mission. The award will be known as the

"James J. Fenton Memorial Award." Its recipient will be someone that epitomizes Mr. Fenton's dedication and many contributions to the auditing and accounting profession.

- o Regional Auditor of the Year Award. To be awarded to one person in each region in grade GS/GM-14 and below who contributes the most during the year to the audit mission of the region.
- o Headquarters Auditor of the Year Award. To be awarded to one person at Headquarters who contributes the most during the year to OA's mission.
- o Staff Person of the Year Award. To be awarded to one non-auditor within OA who contributes the most during the year to OA's mission.

5. Awards Ceremony. An awards ceremony will be conducted annually by the AIGA and Regional Managers to recognize those persons who have made noteworthy achievements during the year. This ceremony will be used to announce awards and bonuses only. Promotions, letters of commendation, or other similar recognitions should not be held up pending the scheduling of an awards program.

G. AUDIT CAREER ADVISORY PANEL

The ACAP advises the AIGA on all personnel management matters pertaining to OA assigned staff. The procedures established for the ACAP are designed to provide an equitable, fair and deliberative approach for identifying and recognizing those persons that have performed in a manner worthy of recognition. For purposes of this policy, recognition includes, but is not limited to, promotions to grades 13, 14 and 15, bonuses and awards, and long-term training. Specific procedures established for the ACAP are described below.

1. ACAP Membership. Members of ACAP shall include the DAIGs and the Regional Managers. The DAIG/AP³ shall function as the Executive Director of the ACAP and, when instructed to do so by the AIGA, shall arrange for the ACAP meetings and brief the AIGA. The DAIG/AO shall act as the ACAP Executive Director in instances in which the DAIG/AP³ cannot function in this capacity.

2. Responsibilities. The DAIG/AP³ shall ensure compliance with the ACAP functions, as described in this chapter. The ACAP members shall execute their mandate in a manner that is fair and equitable to all OA employees and that ensures mission priorities are given adequate consideration. The ACAP shall ensure that personnel actions referred to it by the AIGA for deliberation:

- o Are adequately supported and documented in accordance with this Manual and other pertinent IG personnel policies, DOE Orders, and Federal Personnel Manual procedures, rules and regulations;
- o Are consistent with the tables of organization as approved by the AIGA for each of OA's major organizational elements (in this regard, consideration shall be given to maintaining an appropriate grade structure consistent with OA's mission and organizational structure; and

- o Represent the most qualified and deserving candidate among all OA assigned personnel (for promotions, consideration shall be given to filling valid vacancies from all willing and qualified candidates regardless of their duty station).

3. Frequency and Place of Meetings. The ACAP shall meet as often as needed to complete its assigned functions. While desirable, it is not essential that the panel meet in person. Conference calls are permissible. The ACAP will arrange to meet during every executive workshop. Although a quorum will consist of three members, it is desirable for all members to attend each meeting. Substitutes are not permitted. The Executive Director shall orally notify all members of the agenda items in advance of each scheduled meeting.

4. ACAP Powers. The ACAP shall function in an advisory capacity only. Its recommendations are not binding on the deciding officials.

a. Promotions - Unless otherwise indicated by the AIGA, the ACAP will only consider promotions to grades 13, 14 and 15. Persons in the supervisory chain of command below the AIGA are recommending officials and the AIGA is the selecting official. The DAIGs and Regional Managers are the selecting officials for promotions through grade 12, subject to final approval by the AIGA. Individual recommendations for promotion may be made by the candidate's supervisor through the proper supervisory channels.

b. Bonuses and Awards - The ACAP will consider bonuses and awards at the discretion of the AIGA, and the AIGA shall recommend candidates for awards and bonuses to the IG for approval, in accordance with this Manual, applicable OIG Directives, DOE Orders, and the constraints of available funds.

c. Training - Training requests will be processed through appropriate supervisory channels for preliminary approval or disapproval and will then be forwarded to the AIGA for final approval. The ACAP will consider training requests at the discretion of the AIGA and in accordance with the guidance in chapter 28. Pertinent factors include an employee's current duties and responsibilities, Yellow Book requirements, need, cost, workload, availability of funds, and the impact on or benefit to OA's mission. Once the training has been approved, the AIGA will forward the request to AIGP for authorization and final processing.

5. Communicating With Employees. The results of the ACAP meetings are to be communicated only to the AIGA. Supervisors at all levels, however, are to maintain effective and frequent communications with employees to assist them in their career development. Employees are to obtain information concerning status of personnel action concerning promotions, awards, bonuses, training, etc., through their appropriate supervisory channels. Personnel assistance and information or guidance concerning personnel matters--such as job qualifications, grievances, counseling, equal opportunity, training, performance appraisal procedures, rules, regulations, policies and procedures--may be obtained from AIGP' Human Resources Division.

CHAPTER 27TRAVELA. SCOPE OF CHAPTER

This chapter provides a brief summary of responsibilities, policies, and procedures for approving and conducting official travel.

B. GENERAL POLICY AND CONTROL

DOE Order 1500.2A, "Travel Policy and Procedures," issued 6-7-89, contains official travel policy and procedures for DOE employees. The DAIGs and Regional Managers are responsible for ensuring that travel necessary to accomplish OA's mission is properly approved, is conducted in an effective and economical manner, and complies with the travel procedures contained in the DOE Order as implemented by the AIGP. Travelers also bear responsibility for ensuring that they comply with DOE's prescribed travel procedures.

1. AIGP Travel Administration. In accordance with OIG Directive IG-20B, "Travel Administration," issued 4-6-92, the AIGP is responsible for:

- o Reviewing all travel authorizations (DOE F 1510.1B) to ensure compliance with DOE regulations and the availability of funds. Travel authorizations are to be processed within two working days or less dependent upon the urgency of the travel;
- o Controlling and issuing Government Transportation Requests;
- o Approving blanket travel advances and monitoring the advances on a trip-by-trip basis;
- o Issuing credit card applications;
- o Reviewing and processing correct and complete travel vouchers (SF 1012 and SF 1164) within three working days;
- o Providing a monthly report on travel expenditures to the AIGA, DAIGs, and Regional Managers;
- o Preparing a weekly trip report for the AIGA and DAIGs;
- o Initiating and coordinating all Permanent Changes of Station for OIG personnel; and
- o Advising OIG employees of any changes to the travel regulations, problems with the processing of their travel authorizations, vouchers, and credit cards, and notifying travelers of outstanding travel vouchers or airline tickets.

2. Approving Travel. The DAIGs and Regional Managers are responsible for ensuring that travel authorizations are properly prepared and signed by

the appropriate supervisor and that they are submitted to the AIGP in a timely manner. They are also responsible for ensuring that OA's travel funds are managed in a prudent and efficient manner.

a. Submitting Authorizations - Travel authorizations should be submitted at least three working days prior to the start of the travel. If this is not possible, arrangements should be made within each office to process travel within a day. If the traveler's immediate supervisor is not available to sign the travel authorization, and the person who approved the travel is located at a different office or location, the person's name should be typed on DOE F 1510.1B, Block #22, as the person who approved the travel.

b. Keeping AIGA Informed of Travel - The DAIGs and Regional Managers are responsible for ensuring that the AIGA is kept informed on and has approved all interregional travel regardless of its purpose and travel within a region that is not directly related to a specific audit. The AIGA's Executive Assistant is responsible for coordinating with the AIGP each week to obtain information on approved travel within OA. [Note: Related information on coordination within OA is provided in chapter 5, section D, item 3.(c).]

3. Reimbursement for Travel. Reimbursement for all travel expenses will be in accordance with DOE Order 1500.2A.

a. Responsibilities - It is the employee's responsibility to ensure that all claims for expenses are actually incurred in the performance of travel strictly for official business and that it was performed in the most efficient and economical manner. It is the supervisor's responsibility to review travel claims for conformance with prescribed policies prior to submission for payment.

b. Travel Vouchers - After travel is completed, employees shall promptly submit completed vouchers to their supervisors. Review and approval of travel vouchers by first-level supervisors, who are fully knowledgeable of the traveler's activities, are required and will be considered sufficient approval that the traveler performed the travel as authorized. Supervisors shall ensure that all vouchers are submitted to the AIGP within seven working days after travel has been completed.

c. Local Travel - Reimbursement claims for local travel expenses will be submitted on SF 1164 and must include a statement of the purpose of the travel. These claims may be submitted as incurred for amounts over \$25. Claims for amounts under \$25 should be submitted on a monthly basis.

C. TRAVEL PROCEDURES

Because of the extensive nature of prescribed travel procedures in DOE Order 1500.2A, they are generally not repeated in this Manual. A less formidable compilation of information on travel requirements is contained in a brochure, "Reimbursing You for Your Travel Expenses," issued by the Office of the Controller, June 1989. Each OA traveler should have a copy of this brochure and be familiar with its contents. Although not a comprehensive listing, the following items are provided to remind travelers of particularly relevant OIG, DOE or other Federal policies that may apply to them while they are in a travel status.

1. Auto Accidents. Travelers involved in an accident resulting in personal injuries or property damage while driving a privately-owned, government-owned, or rented vehicle on official business shall, unless incapacitated, immediately notify their Regional Manager of the accident. They are also responsible for preparing (1) a Standard Form 91, "Operator's Report of Motor Vehicle Accident," and (2) form CA-1, "Federal Employees Notice of Traumatic Injury and Claim," and forwarding these items to their Regional Manager in an expeditious manner.

2. Local Travel. Travel authorizations are not required for travel performed within a 50-mile radius of an employee's official duty station. In addition to the use of a privately owned vehicle and other local transportation costs, telephone calls, telegrams, registration fees, parking expenses, etc., are claimed on the local travel form (SF 1164). Local travel is not to be used to obtain supplies and other items that should go through procurement. Travel authorizations may be issued for travel within the local area when an employee is to remain away from home overnight, or to attend conferences or meetings that require the payment of a registration fee of \$50 or more.

a. Local travel expenses will include only those expenses necessary for the performance of assigned duties. Mileage or other local transportation costs between an employee's home and temporary duty sites may be claimed to the extent it exceeds the normal commute between home and official duty station. For purposes of computing normal commuting costs, car pool members may divide their commuting mileage by the number of regular members in the car pool.

b. Travel between work sites will be by DOE shuttle or local transportation whenever practicable. Use of taxis for such travel will be on an exception basis only, and must be justified by the traveler.

3. Phone Calls. Travelers are authorized to make brief long distance calls to their family or residence when in a travel status for at least two nights. The maximum number of calls that may be authorized is an average of one per day, with the maximum amount that may be approved for reimbursement to be \$12 per trip, or each consecutive 7-day period of a single trip, not to exceed a cost of \$4 a call. Travelers are also authorized to make long distance calls to notify their families of transportation delays or changes in their travel schedule.

4. Receipts. Travelers shall obtain and submit receipts for all cash expenditures in excess of \$25 plus any applicable tax. Receipts are required for the following expenditures, regardless of cost:

- o Freight shipments, excess baggage, and baggage transfer, checking and storage charges;
- o Clerical assistance and fees for copies of records furnished by State officials (e.g., clerks of courts);
- o Hire of special conveyances such as boats, motor vehicles (other than taxis), and aircraft;

- o Operating expenses--such as gas, oil, and garage rental--for rented vehicles and special conveyances;
- o Telegrams and long distance telephone calls (except where a coin operated telephone is used and it is so stated in the travel voucher); and
- o Cash payments for passenger transportation services (except for taxis or local transportation, such as a bus or streetcar, used in lieu of a taxi).

5. Rental Cars. Travelers obtaining rental cars are reminded that the Government will not pay or reimburse employees for the cost of the collision damage waiver or collision damage insurance available for an extra fee in commercial rental contracts. If this fee is automatically added, it is the traveler's responsibility not to incur the charge since Government rate agreements already include full comprehensive and collision coverage.

6. Tax Exemption Certificates. There are some locations that offer specific exemptions to individual Federal employees for payment of State and local lodging occupancy taxes. The tax jurisdictions known to offer exemptions are identified along with their procedural requirements in the Federal Travel Directory.

Federal employees on official travel should claim an occupancy tax exemption in those jurisdictions where a specific exemption exists. Claims are to be made in accordance with the procedures required by the tax jurisdiction. However, OA employees are instructed not to attempt to use makeshift tax exemption forms or to claim exemptions to which they are not entitled. A copy of the exemption certificate that is normally used is illustrated in exhibit A (A:AM27EXA.WPF).

TO BE RETAINED BY OPERATORS OF HOTEL, EXEMPTION CERTIFICATE
MOTELS, AND SIMILAR ACCOMMODATIONS AS TAX ON OCCUPANCY OF HOTEL ROOMS
EVIDENCE OF EXEMPT OCCUPANCY

NAME OF HOTEL, APARTMENT HOTEL, OR LODGING HOUSE _____ DATE _____

ADDRESS

This is to certify that I, the undersigned, am a representative of the United States Governmental department, agency or instrumentality indicated below; that the charges for the occupancy at the above establishment on the dates set forth below have been or will be paid for by such governmental unit; and that such charges are incurred in the performance of my official duties as a representative or employee of such governmental unit.

DATES OF
OCCUPANCY _____ (SIGNATURE)
GOVERNMENTAL
UNIT _____ (TITLE)

NOTE - A SEPARATE EXEMPTION CERTIFICATE IS REQUIRED FOR EACH OCCUPANCY AND FOR EACH REPRESENTATIVE OR _____ EMPLOYEE

CHAPTER 28PROFESSIONAL DEVELOPMENTA. SCOPE OF CHAPTER

This chapter provides detailed policies and procedures for professional development and training.

B. YELLOW BOOK REQUIREMENTS

According to the Yellow Book, auditors responsible for planning, directing, conducting, or reporting on government audits should complete, every 2 years, at least 80 hours of continuing education and training which contributes to the auditor's professional proficiency. At least 20 hours should be completed in any one year of the 2-year period. Individuals responsible for planning, directing, conducting substantial portions of the field work, or reporting on the government audit should complete at least 24 of the 80 hours of continuing education and training in subjects directly related to the government environment and to government auditing.

This chapter describes the procedures for achieving that compliance with these requirements. Of equal importance, however, is OA's goal to provide training opportunities that meet specific needs and contribute directly to attaining individual and organizational excellence. To that end, this chapter also describes a training system designed to go beyond mere "clocking" of hours and encourage the development of motivated, well trained, highly qualified, interdisciplinary professional auditors.

C. TRAINING REFERENCES

The training requirements outlined in this chapter deal primarily with policy and procedures incident to the Yellow Book. OA staff should also be aware, however, of the following additional criteria.

1. Departmental Training Order. DOE Order 3410.1B, "Training," issued 2-29-89, provides departmental policies and responsibilities for employee development and training programs and activities.

2. Office of Inspector General Directive. OIG Directive IG-13B, "Training," issued 6-22-89, defines responsibilities and sets procedures for implementing the OIG employee development and training program. This directive discusses the role of AIGP and the OIG Training Officer. The Training Officer is a resource upon which OA must rely heavily. The Training Officer's responsibilities include

- o interpreting OPM and DOE policy issuances and directives regarding training;
- o providing advisory services to OIG supervisors, managers, and other employees on the full range of training matters;

- o providing oversight for all administrative aspects associated with training; and
- o informing employees promptly of approval/disapproval of training requests.

D. RESPONSIBILITIES FOR TRAINING AND CONTINUING EDUCATION

Assuring compliance with continuing professional education (CPE) requirements requires a multi-tiered approach involving the individual auditor, supervisors, regional training coordinators, and AP3. The responsibilities of each are detailed below.

1. Auditors. Each auditor is expected to seek--and successfully complete--training appropriate to his or her grade level, experience, likely audit areas, and personal development goals. Auditors should discuss their training needs and preferences with their supervisors. They should also consult with their regional training coordinator to determine course offerings and availability. To formalize this process, auditors must annually (by September 1) complete an Individual Development Plan (IDP) detailing desired training. The IDP, illustrated in exhibit A (A:AM28EXA.WPF), requires auditors to identify short-term (one year) and long-term development objectives and to request specific courses or programs designed to help achieve those objectives. Examples of development objectives that could be identified are

- o attaining professional certification;
- o gaining expertise in a relevant functional area (e.g., procurement); or
- o increasing knowledge in a relevant program area (e.g., solar energy).

IDPs should be signed by the employee and supervisor. The auditor should keep the original and submit a copy to the regional training coordinator. The training coordinator will, in turn, forward a copy to AP3. IDPs serve the dual purpose of encouraging auditors to plan their individual development and allowing the OIG to fulfill its obligation to annually assess training needs.

IDPs are intended to be a tool to help auditors plan and develop their careers. They are also intended to help AP3 and AIGP identify training needs. While requested training should usually be identified in or directly relate to the objectives established in the IDP, this will not always be the case. Training requests will not be denied simply because the requested course is not specifically identified in the IDP; however, no training will be approved unless an IDP has been submitted.

Auditors are also responsible for retaining documentation for each course or training program completed. Although regional training coordinators and AP3 will maintain some information on courses taken and progress toward meeting CPE requirements, ultimate responsibility for documenting participation in training will reside with the individual auditor. Acceptable documentation includes

- o records of course grades;
- o outlines and evidence of attendance; or
- o certificates of completion from program sponsors.

GAO guidance issued in April 1991 states that CPE records should be maintained for an appropriate period of time to satisfy legal and administrative requirements. OA auditors, for their own benefit and future reference, should probably retain the information indefinitely.

2. Supervisors. Supervisors are expected to take a proactive role in the training and development of the auditors who report to them. As part of the IDP process and throughout the year, supervisors should (1) act as an advocate for the auditor, suggesting goals and training beneficial to the individual, and (2) represent the interests of OA, encouraging the development of skills and abilities that are critical to the office. Supervisors should also help auditors identify areas of needed improvement and suggest training in those areas. Although not required, auditors and supervisors may wish to discuss and revise IDPs as part of mid-point performance evaluations.

3. Regional Training Coordinators. Each Regional Manager will appoint a regional training coordinator. Regional training coordinators are responsible for

- o maintaining up-to-date IDPs for every auditor in the region and annually forwarding copies of the IDPs to AP3;
- o assuring that the Training Information Management System (TIMS) is accurate for the region and periodically submitting TIMS reports to AP3 (TIMS is discussed below);
- o establishing and maintaining current information on course offerings, schedules, and vendors (see exhibit B, A:AM28EXB for a list of training sources);
- o acting in an advisory capacity to assist auditors and supervisors in preparing development objectives and choosing appropriate training to achieve those objectives; and
- o acting as principal liaison between the region and AP3 for all matters related to training.

4. Headquarters Coordination. AP3 functions as the regional training coordinator for all Headquarters auditors and as the liaison between the regions and AIGP. In addition, AP3 monitors, through periodic TIMS reports from the regions, the progress of all OA auditors toward complying with Yellow Book CPE requirements. AP3 will also periodically review each region's CPE tracking procedures and documentation to assure compliance.

E. TRAINING REQUEST PROCEDURES

To the extent feasible considering budget constraints and office priorities, OA will provide financial support for relevant training. The following

procedures should be followed in requesting such training.

1. Training Request Form. At least 6 weeks prior to the scheduled start date of desired training, the employee should submit the preliminary training request form (IG-TF-1), as illustrated in exhibit C (A:AM28EXC. WPF). This form is submitted to the supervisor for approval and then to the regional training coordinator who certifies, by initialing the form, that the training is

- o consistent with this Manual; and
- o cost effective regarding location and provider of training.

Backup information (brochures, etc.) about the course should be attached.

2. Travel Arrangements and Registration. After all local approvals have been obtained, the request form is mailed to AP3 which obtains the necessary approval from the AIGA. At the same time, the audit office secretary shall make the necessary hotel/motel, rental car, and transportation requests. Course registration is AIGP's responsibility, acting on the AIGA's approval of the training request. Travel authorization should accompany the preliminary training request form to AP3.

3. Late Submissions. The regional training coordinator will notify AP3 by E-Mail message of training requests submitted less than 4 weeks prior to the scheduled training start date. The official training request form will be prepared and processed in accordance with the above procedures.

4. Cancellations. The regional training coordinator will also notify AP3 by E-Mail of cancellation of employee's attendance at previously scheduled training, and the reason for cancellation.

F. TRAINING REQUIREMENTS AND RECORDS

Requirements for obtaining and recording training or other continuing professional education are described below.

1. Recording Training for Credit. Upon completion of the training, AIGP will send the auditor the "goldenrod" course evaluation form. The auditor should complete this form and submit it to the regional training coordinator. The training coordinator will then assure that Yellow Book credit is recorded in TIMS and forward the goldenrod form to AP3. For courses or training where no goldenrod form is generated, regional offices should develop alternative methods for recording credit.

2. Training Information Management System. TIMS is a database which maintains information on training and professional development activities in order to ensure that OA training policies and Yellow Book requirements are met. TIMS accumulates information on training plans and training courses completed. Instructions for using TIMS are contained in the TIMS Users Guide, distributed to regional training coordinators.

Each Regional Office must implement a system to ensure that required training information is entered into TIMS in a timely manner. Regional

training coordinators are responsible for assuring that TIMS is current and accurate for their region. A recommended approach is for employees to complete the "goldenrod" evaluation form, have it signed by their supervisor, and submit it to the regional training coordinator immediately following completion of the training. The goldenrod form should then be forwarded to AP3.

OA anticipates that TIMS will eventually become the basis for a training module within the IGDBMS.

3. Training History Records. In order to better assist auditors in choosing the appropriate training over the years, regional coordinators may choose to track, on a long-term basis, training that has been accomplished by each auditor. A sample career development record and training history form is provided as exhibit D (A:AM28EXD.WPF) to this chapter. This form is optional.

4. Measurement Period. The measurement period for meeting Yellow Book CPE requirements runs on a 2-year cycle. An initial period began 10/1/88 and ran until 9/30/90, with subsequent periods every 2 years thereafter.

5. Deficiency Make-Up. A deficiency in meeting the CPE requirements should be rare. However, should such a deficiency occur, GAO's draft guidance is that the auditor will have 2 months immediately following the 2-year period to make up the required hours. Any CPE hours completed toward a deficiency in one period may not be counted toward the requirements for the next 2-year period. GAO guidance states that auditors who, after the 2-month grace period, still have not satisfied the CPE requirements will not be permitted to participate in audits until those requirements are satisfied.

6. Requirements for Newly Employed Auditors. Auditors who have been employed by OA for less than one year of a given 2-year period are not required to obtain a minimum number of CPE hours. Auditors who have been employed at least one year, but less than 2, in a given 2-year period are required to earn a minimum of 20 CPE hours.

7. Determining What Qualifies for Credit. GAO's interpretation defines CPE programs as structured educational activities designed to maintain or enhance participants' knowledge and skills in areas applicable to the discipline in which they work. The interpretation states that auditors should have wide latitude in selecting suitable CPE. According to GAO, the following types of training may be acceptable.

- o Internal training programs.
- o Audit organization staff meetings when a structured educational program is presented.
- o University and college courses.
- o Education and development programs presented at conferences, conventions, meetings, seminars, and workshops of professional organizations.
- o Training programs presented by other audit organizations, educational organizations, foundations, and associations.

- o Correspondence courses for which registration is required and evidence of completion is provided by the sponsor.
- o Courses given through audio tapes, video tapes, and computers.
- o Other professional activities, such as speaking, teaching courses that qualify for CPE, and publishing articles that contribute directly to the author's professional proficiency.

a. Number of Hours Granted - Most sponsoring organizations will recommend the number of hours of CPE credit to be granted for a given training program. Where this is not the case, GAO's guidance is that 1 CPE hour should be granted for each 50 minute "contact hour" of participation in qualified training. For university and college courses, each semester hour equals 15 CPE hours; each quarter hour equals 10 CPE hours. Regional training coordinators should seek guidance from AP³ where there is a question regarding hours to be credited.

b. Classifying Training - Regional training coordinators are responsible for seeing that the IG-TF-1 indicates whether the requested training qualifies for the 80 hour CPE requirement and the 24 hour government-related requirement. Training coordinators should seek guidance from AP³ if unsure about classifying particular courses. Although such situations should be rare, where uncertainty regarding classification persists, the DAIG/AP³ will make the final determination.

GAO's interpretation offers the following guidance on classifying training:

- o 80-Hour Requirement - Examples of subjects and topics that may maintain or enhance auditors' knowledge and skills in areas applicable to the discipline in which they work include: accounting principles and standards; analytical procedures; assessment of internal controls; audit methodologies; audit risk and materiality; audit standards; compliance with laws and regulations; budgeting; computer science; contracting and procurement; cost accounting; data analysis; economics; evaluation design; financial management; financial reporting; forecasts and projections; industrial engineering; interviewing techniques; mathematics; operations research; oral and written communication; pension accounting; principles of management and supervision; probability; productivity; program evaluation; public administration; public finance; public policy and structure; quality control; report writing; social sciences; sampling; taxation; and workpaper preparation.
- o 24-Hour Government Requirement - Examples of subjects and topics that may maintain or enhance the auditor's knowledge and skills to audit in the government environment include: government accounting principles; budgeting; procurement and contracting in government; legislative policies and procedures; effects of current economic conditions on government operations; relevant laws and regulations; and government program and service performance measurement and reporting.

G. PROFESSIONAL DEVELOPMENT CURRICULUM

OA has designed a professional development curriculum for auditors. The curriculum is illustrated in exhibit E (A:AM28EXE.WPF). Curriculum objectives and components are discussed below.

1. Curriculum Objectives. The OA Professional Development Curriculum is intended to encourage overall career planning and thoughtful selection of individual training opportunities. Auditors should consult the curriculum for a basic understanding of the training they should complete and the skills they should master at each career level. When fully implemented, the curriculum will also allow OA to assure that auditors meet the 80-hour CPE requirement in an efficient and cost-effective manner. This will be accomplished by specifying certain courses as required, standardizing course objectives, centralizing course scheduling, and assuring that OA trainers are themselves well trained in the subject matter and in educational techniques. AP³ works in cooperation with the regional training coordinators to develop and maintain the curriculum, and to schedule training.

2. Required Courses. Required courses make up the curriculum's first tier. Currently, required courses include those specified in the First-Year Program (discussed in section H below) and a series of writing courses. Additional required courses may be added in the future. Auditors and supervisors should work together to assure that required courses are scheduled and completed at the indicated grade levels.

3. Core Courses. There are a number of skills that OA believes auditors should possess at each career level. The most important of these skills are outlined in the Auditor Skills Profile, presented in exhibit F (A:AM28EXF.WPF). Although OA may not require specific courses for each skill or category of skills, auditors are expected to master the skills through classroom or OJT. A core course, therefore, is one that is not required but that addresses one or more of the skills on the Auditor Skills Profile. Auditors and supervisors should periodically review the listed skills and identify any developmental needs. Where appropriate, in-house or contract courses should then be requested to address those needs.

4. Regional Rotational Courses. Over the past several years, OA regional offices and Headquarters have developed a number of training courses in various auditing disciplines, including evidence, referencing, and detection of illegal acts. In the past, auditors in one region have generally not been aware of the course offerings in another. In 1994, these courses will be centrally scheduled so that all OA auditors can be aware of and, where feasible, take advantage of course offerings. These courses are referred to as regional rotational courses in that their timing and location will be scheduled on a rotating basis to meet identified needs.

Regional Offices are encouraged to continue developing in-house training in areas of identified need where it is feasible and cost-effective to do so. This must be done in cooperation with AP³, however, so that training quality, consistency, and efficiency can be assured. AP³ will require that, at a minimum, proposed in-house training courses meet the following criteria, as listed in GAO's guidance.

- o An agenda or outline is prepared in advance and retained that indicates the name of the instructor, subject covered, program learning objectives, and any prerequisites.
- o The program is developed by individuals qualified or experienced in the subject matter.
- o Program materials are technically accurate, current and sufficient to meet the program's learning objectives.
- o Programs are reviewed, when appropriate, by other qualified or experienced individuals.
- o Evaluations of the program are obtained from instructors and participants.

5. Issue Area Seminars. The fourth tier of OA's professional development program is intended to provide auditors with current knowledge of various DOE activities and programs. As part of the annual planning process, AP³ and the regional training coordinators will identify areas of need or special interest. For example, there may be a need for auditors at certain locations to receive training in a new DOE program. Once such need are identified, AP³ will schedule training seminars with Departmental officials or other knowledgeable individuals. Issue area seminars will be held at various sites and be targeted to specific audiences.

6. Elective and Special Courses. There may be courses that auditors need or want to take that do not fall into one of the other curriculum tiers. Examples include certification review courses, specialized computer training, or executive development programs. These special and elective courses should help the auditor meet at least one IDP objective and should be cost-effective.

H. FIRST-YEAR PROGRAM

During their first year with OA, newly hired auditors participate in a formalized training program, consisting of both classroom participation and on-the-job training (OJT). The major components of the first-year program are described below.

1. Classroom Training. Formal classroom training for first-year auditors generally includes 3 days of orientation to the OIG and DOE, three weeks of "Introduction to Government Auditing" at the IG Auditor Training Institute, and additional courses in word processing applications, writing skills, and fraud awareness. Other courses may also be offered.

2. On-the-Job Training. OJT is as vital to an effective training program as formal training. It is an effective tool in developing staff because it provides the opportunity to apply and reinforce, under supervision, the skills learned in formal training. In that respect, supervisors should be cognizant that an important part of their responsibility is to provide development opportunities and guidance to their employees. Staff rotation may be used as a part of OJT in order to expose firstyear employees to a variety of assignments.

a. General Guidance - OA's OJT Program for new auditors is intended to formally plan and recognize learning which takes place through on-the-job work experience. Ensuring that OJT is effectively implemented is a joint responsibility of the appraising official, usually an Audit Director, and the AIC on the audit to which the employee is assigned. New auditors should be encouraged to seek the fullest possible range of OJT experience on each audit assignment and to speak up if they feel that any OJT task is being omitted from their experience. OJT is intended to complement and enhance formal training but is not a substitute for it.

b. Suggested Implementation of OJT - A one-page OJT performance record is provided for appraising officials to track the progress of new auditors (see exhibit G, A:AM28EXG.WPF). Space is provided for the appraising official to date and initial satisfactory completion of each OJT task, as advised by the new auditor's immediate supervisor and/or sponsor. In the event that an appraising official concludes that, having been given sufficient opportunity, the new auditor has not completed an OJT task at a satisfactory level, the appraising official must make a notation of the course of action proposed to help the new auditor achieve the task at the satisfactory level.

Supervisors should complete OJT Performance Records monthly during the auditor's first year and submit them to the regional training coordinator. If the auditor is recommended for accelerated promotion, promotion documentation submitted to AP³ must include OJT Performance Records indicating that at least nine of the 18 tasks have been successfully completed.

3. Sponsorship. As they come on board, OA's entry-level auditors are assigned a more seasoned OA employee to help them make the transition from college student to confident professional. The sponsor's role is primarily personal rather than supervisory. Sponsors help new auditors become acquainted with their surroundings on the job and provide informal counseling. Many sponsors have also volunteered hours of their own time to show relocated new hires around the community and assist in housing searches.

I. WRITING ASSESSMENT PROGRAM

To assure that our auditors become comfortable and confident professional writers, OA has instituted a writing assessment program. Entry level auditors progress through the professional development curriculum's required writing courses--and, as needed, personalized instruction-- building a writing "portfolio" as they go. Before they can be considered for promotion to GS-12, auditors must have their portfolios evaluated by a panel of senior OA employees. The portfolios must demonstrate that the auditor has mastered OA's professional writing standards, including the deductive writing style. The portfolio approach serves the OA objective to produce high quality written products, and does so in a constructive and non-threatening manner. Knowing that their portfolios will ultimately be judged motivates OA employees to give great attention to the quality of their written products.

1. Writing Portfolio. GS-11s wishing to be considered for promotion to GS-12 will provide a portfolio--containing at least 3 but not more than 6 writing samples--to AP³. Writing samples that may be included are interview writeups, summaries, tentative findings, audit report segments, or other

documents that demonstrate competency in the deductive writing style. (Published reports cannot be accepted.) The portfolio should include lead and supporting paragraphs with topic sentences and the elements of a finding (criteria, condition, cause, effect). To the extent possible, names of DOE locations, contractors, and other identifying information should be deleted to assure confidentiality.

2. Certification. Auditors will certify, by their signature, that the portfolio represents their own writing. Documents need not be "first drafts" and may reflect the comments and suggestions of supervisors.

3. Review Timeframe. GS-11s may submit the portfolio to AP³ at any time but should allow a minimum of 60 days for review.

4. Identifying Numbers. AP³ will assign identifying numbers to portfolios and will forward them to a panel of three GS/GM-14/15s who have been trained in the deductive style and in the evaluation techniques to be used. Panel members will not be from the same region as the candidate.

5. Blind Panel. Panel members will not know whose work they are evaluating or the names of other panel members. They will complete evaluation/comment sheets and indicate whether or not each writing sample demonstrates competency. The evaluations will be independently done by each panel member without consulting with anyone. Portfolios and evaluation sheets will then be returned to AP³.

6. Successful Completion. Auditors will have successfully demonstrated their deductive writing competency if the evaluations of the portfolios so indicate. To assure fairness, AP³, in consultation with the technical consultant, will review the panel's evaluations to assure that each evaluating panel member has satisfactorily applied the evaluation techniques. The final determination on each portfolio will be made by the Deputy Assistant Inspector General for Audit Policy, Plans & Programs. AP³ will assure that all auditors are counseled as to the strengths and weaknesses of their portfolios.

7. Unsuccessful Portfolios. Auditors who do not successfully demonstrate their writing competency will be counseled as to needed improvements and will be given the opportunity to resubmit enhanced portfolios for evaluation by a different panel.

8. Impact on Promotion to GS-12. Successful demonstration of writing competency is a requirement for, but does not guarantee, promotion to GS-12.

9. Confidentiality. Every effort will be made to assure confidentiality. Results of the assessment will be discussed only among the auditor, the AP³ project coordinator/technical consultant, and those members of OA management that need to know. All envelopes containing correspondence will be appropriately marked to assure confidentiality.

J. PROFESSIONAL CERTIFICATION

Professional certification, such as Certified Public Accountant (CPA), Certified Internal Auditor (CIA), and Certified Information Systems Auditor (CISA), is a mark of professional excellence and stature for auditors and for

the audit organization. Auditors are strongly encouraged to pursue certification. OA will assist auditors in attaining certification as described below.

1. Payment for Review Courses. Subject to the availability of funds, OA will pay the cost of an approved review course, including tuition, fees, books, and course materials (Note: Travel expenses will not be reimbursed). Such courses must be completed on the employee's off-duty time. For auditors who have been employed by OA less than 1 year, payment for review courses requires approval by the Inspector General and is contingent upon the completion of a continued service agreement. OA will pay for such courses once per auditor, and the auditor is required to sit for the next scheduled examination after completing the course.

2. Requirements for Certified Public Accountants. Auditors who hold CPA licenses should be aware that meeting Yellow Book CPE requirements may or may not satisfy state licensing agencies. OA will provide reasonable assistance to certified auditors to help them meet state CPE requirements.

K. TRAINING FOR NON-AUDITORS

Although Yellow Book standards do not provide specific educational requirements for non-auditors, OA policy is that relevant training opportunities be encouraged and made available to all staff. Secretaries, administrative support personnel, and other specialists are extremely valuable resources without whom OA could not function effectively. Regional offices should design and implement procedures to assure their non-auditor staff members receive relevant professional education. AP³ will also be involved in this process, identifying appropriate external training sources and periodically scheduling inhouse training opportunities.

L. EXTERNAL STAFF QUALIFICATIONS

If contracted audit services or other external staff are utilized on an audit, it will generally be the contractor's responsibility to assure that the assigned staff have the requisite qualifications and training. However, OA will consider the experience, training, and qualifications of contractor audit personnel when selecting contract audit services and in assigning tasks or audits to the contractor. In addition, external auditors selected to perform financial statement audits that lead to an expression of an opinion must have the following qualifications, as required by the Yellow Book:

- o The auditor should be proficient in the appropriate accounting principles and standards and in government auditing.
- o Public accountants engaged to conduct audits should be (1) licensed CPAs or persons working for a licensed CPA firm, or (2) public accountants licensed on or before December 31, 1970, or persons working for a public accounting firm licensed on or before December 31, 1970.

See chapter 5, section D, item 4, for additional discussion on staffing considerations.

**OFFICE OF INSPECTOR GENERAL
INDIVIDUAL DEVELOPMENT PLAN**

EMPLOYEE:	SSN:	OFFICE	POSITION TITLE	START DATE	FY END DATE
EMPLOYEE SIGNATURE/DATE	SUPERVISOR SIGNATURE/DATE	2ND LEVEL SUPERVISOR SIGNATURE/DATE		HRMD REVIEW/DATE	
PURPOSE:		DIRECTIONS: 1. STATE OBJECTIVE AS SPECIFIC GOAL 2. UNDER "HOW ACCOMPLISHED" SPECIFY ACTION TO BE TAKEN FOR EACH OBJECTIVE: ROTATIONAL ASSIGNMENT OJT, CONFERENCES, TRAINING COURSE.		PRIORITY: 1. REQUIRED TO PERFORM, OR MORE EFFECTIVELY PERFORM, CURRENT OR FUTURE DUTIES IN SAME POSITION. 2. REQUIRED BY LAW, RULE OR REG. 3. PROVIDE FOR REPLACEMENT OF EMPLOYEES THRU DEVELOPMENT PROG. 4. OTHER (EXPLAIN)	
SHORT-RANGE PLAN (CURRENT FY)					
DEVELOPMENTAL OBJECTIVE	PRIORITY	EST.COST	HOW ACCOMPLISHED	ACTION	

LONG-RANGE PLAN				
DEVELOPMENTAL OBJECTIVE	PRIORITY	EST.COST	HOW ACCOMPLISHED	ACTION

CORE LIST OF TRAINING SOURCES

American Institute of Certified Public Accountants
1211 Avenue of the Americas
New York, NY 10036-8775
(212) 575-6200

State CPA Societies

Colorado Society of CPAs
Building 46B
7720 E. Belleview Avenue
Englewood, Colorado 80111

DC Institute of CPAs
1666 K Street, NW
Washington, DC 20006

Maryland Association of CPAs
1300 York Road, Suite 10
P.O. Box 484
Lutherville, Maryland 21093 (301) 296-6250

New Mexico Society of CPAs
300 San Mateo, NE #101
Albuquerque, New Mexico 87108

Tennessee Society of CPAs
200 Powell Place - Suite 120
Box 596
Brentwood, TN 37024-0596

Texas Society of CPAs
P.O. Box 300008
Dallas, Texas 75303-0008

CPA Review Courses

Becker CPA Review
15760 Ventura Blvd #1101
Encino, California 91436

Borra CPA Review
8321 Commanche Court
Bethesda, Maryland 20817

Lambers CPA Review
157 Central Street N
Reading, Massachusetts 08164

Totaltape CPA Review
9417 Princess Palm Avenue
Tampa, FL 33619

Conviser Duffy
1415 Fannin, Suite 250
Houston, TX 77006

American Management Association
P.O. Box 319
Saranac Lake, NY 12983

Association of Government Accountants
601 Wythe Street
Suite 204
Alexandria, VA 22314
(703) 684-6931

AT&T
Education and Training
55 Corporate Drive
Room 13C66
Bridgewater, NJ 08807-9903

The Brookings Institution
1775 Massachusetts Avenue, N.W.
Washington, D.C. 20036-2188

Career Development Institute
1550 East 78th Street
Richfield, Minnesota 55423

Career Vision, Inc.
251 Park Avenue, South
12 Floor
New York, NY 10003

Center for Applied Management
Room 108
600 Maryland Avenue, S.W.
Washington, D.C. 20024-2520

Center for Public Management
12713 Steeple Chase Way
Potomac, MD 20854

Colleges and Universities

Augusta College
2500 Walton Way
Augusta, Georgia 30910

Aurora College
Denver, Colorado 80204

Chapman College
Kirtland AFB

Albuquerque, New Mexico 87117

Clark Community College
3200 E. Cheyenne Avenue North
Las Vegas, Nevada 89030

Clemson University
P.O. Drawer 912
Clemson, South Carolina 29631

Frederick Community College
7932 Opossumtown Pike
Frederick, Maryland 21701

George Mason University
Herndon, Virginia 22071

Georgetown University
Washington, DC 20057

George Washington University
2121 I Street, NW
Washington, DC 20052

Illinois-Benedictine College
Lisle, Illinois

Massachusetts Institute of Technology
Cambridge, Massachusetts 02139

Montgomery College
900 Hungerford Drive
Rockville, Maryland 20850

Northern Virginia Community College
8333 Little River Turnpike
Annandale, Virginia 22003

Prince George's Community College
301 Largo Road
Largo, Maryland 20772

Tri Cities University
100 Sprout Road
Richland, Washington 99352

University of Maryland
College Park, Maryland 20742

University of New Mexico
Albuquerque, New Mexico 87131

University of South Carolina
Columbia, South Carolina 29208

University of Tennessee
2014-1016 Lake Avenue
Knoxville, Tennessee 37996-3910

Washington State University
390 Hanford Street
Richland, Washington 99352

Computer Learning Center
134 North Peters Road
Knoxville, TN 37923

Data-Tech Institute
Lakeview Plaza
P.O. Box 2429
Clifton, NJ 07015

Defense Contract Audit Agency
Cameron Station
Alexandria, VA 22304-6178

Department of Non-Credit Programs
Division of Continuing Education
The University of Tennessee
Knoxville, TN

EDP Auditors Association/EDP Auditors Foundation
455 East Kehoe Blvd., Suite 106
P.O. Box 88180
Carol Stream, IL 60188-0180
(312) 653-0950

Executive Enterprises, Inc.
22 West 21st Street
New York, NY 10010-6904

Federal Executive Institute
Office of Personnel Management
1301 Emmet Street
Charlottesville, VA 22901
FTS 940-6200 or (804) 980-6200

General Accounting Office
Special Programs Branch
GAO Training Institute
Washington, DC 20548
FTS 275-9252 or (202) 275-9252

General Service Administration Training Center
P.O. Box 15608
Arlington, VA 22215-0608
FTS 557-0987 or (703) 557-0987

Government Audit Training Institute
Graduate School, USDA
Room 138
600 Maryland Avenue, S.W.
Washington, DC 20024
(202) 382-8620

Graduate School, USDA
Information Office
600 Maryland Avenue, S.W.
Washington, DC 20024
(202) 447-4419

Institute for Advanced Technology
7401 Metro Boulevard, Suite 500
Minneapolis, MN 55435

Institute of Internal Auditors
249 Maitland Avenue
Altamonte Springs, Florida 32715-1119
(305) 830-7600

Management Concepts, Inc.
1964 Gallows Road
Vienna, VA 22182

National Academy of Public Administration
1120 G Street, NW
Washington, DC 20005

National Intergovernmental Audit Forum
General Accounting Office
Attn: Roger Hayman
441 G St., N.W., Room 6124
Washington, DC 20548
FTS 275-9355 or (202) 275-9355

Office of Personnel Management

Atlanta Regional Training Center
Richard B. Russell Federal Bldg.
75 Spring Street, S.W.
Atlanta, GA 30303-3019
FTS 242-3488 or (404) 331-3488

Chicago Regional Training Center
John C. Kluczynski Federal Bldg.
230 N. Dearborn St., 30th Floor
Chicago, IL 60604
FTS 353-2919 or (312) 353-2919

Dallas Regional Training Center
1100 Commerce Street
Dallas, TX 75242
FTS 729-8245 or (214) 767-8245

Philadelphia Regional Training Center
Wm. J. Green, Jr. Federal Bldg.
600 Arch Street
Philadelphia, PA 19106-1596
FTS 597-2527 or (215) 597-2527

San Francisco Regional Training Center
120 Howard Street, 2nd Floor
San Francisco, CA 94105
FTS 454-7700 or (415) 974-7700

OPN Executive Seminar Centers

Central Executive Seminar Center
Broadway Building
301 Broadway Street
Oak Ridge, TN 37831-3515
FTS 626-1730 or (615) 576-1730

Eastern Executive Seminar Center
U.S. Merchant Marine Academy
Kings Point, NY 11024
FTS 663-8811 or (516) 773-5800

Western Executive Seminar Center
1405 Curtis
Denver, CO 80202
FTS 564-6181 or (303) 844-6181

President's Council on Integrity and Efficiency
Office of Management and Budget
Room 252, OEOB
Washington, DC 20503
FTS 395-4000 or (202) 395-4000

Quorum Books Business
An Imprint of Greenwood Publishing Group, Inc.
88 Post Road West
Box 5007
Westport, CT 06881

Initiating Office Date Rec'd ____ IG/EXD in EXD ☒ AIG-A ____ AIG-Inv.	Form IG-TF-1
OFFICE OF INSPECTOR GENERAL Preliminary Training Form	
1. Name _____	2. Number of Yellow Book Hours: _____
3. SSN _____	This course _____ To Date* _____
4. Office Number (FTS) _____	* Current 2-Year Measurement Period
5. Catalog Number _____	Meets 24-hour (Yes) _____ (No) _____
6. Course Title _____	
7. Objectives _____	
(NTE 2 typewritten lines)	
8. Course Start Date _____ (Expressed YY/MM/DD)	Course End Date _____ (Expressed YY/MM/DD)
Number of Duty Hrs. _____ (Expressed 0040)	Number of Non-duty Hrs. _____ (Expressed 0040)
9. Sponsoring Organization's Name _____	
Address _____	
Location of Training _____	
10. Tuition Cost _____	11. Travel _____
Book Fee _____	Per Diem _____
Other Costs (Specify) _____	Other (Specify) _____
Total Cost _____	Total Travel Cost _____
12. Approvals (Authorizing Signatures)	
Immediate Supervisor _____	_____
Name/Title	Date
2nd Level Supervisor _____	_____
Name/Title	Date
13. Did you change organizations recently? Yes No	
New Organization _____	
14. (DOE courses only) 2nd Choice _____	
Prerequisite course taken _____	
Date	Course Title
Regional Training Coordinators should initial completed form in the box at right and return to AP3.	

CAREER DEVELOPMENT RECORD AND TRAINING HISTORY

1. Name: _____ 2. Audit Group: _____

3. SSN: _____ 4. Series/Grade: _____

5. Degrees Held:

<u>Degree</u>	<u>University/College</u>	<u>Year</u>	<u>Major</u>
---------------	---------------------------	-------------	--------------

6. Professional Certificates Held:

() CPA: State _____	Certificate No. _____	Date: _____
() CIA: Certificate No. _____		Date: _____
() Other: Type _____		Date: _____

7. Memberships in Professional Organizations:

<u>Name of Organization</u>	<u>Office/Committee/Activity</u>
-----------------------------	----------------------------------

8. List of Training Courses Completed:

<u>Course Title/Vendor</u>	<u>Code*</u>	<u>Hours</u>	<u>Start Date</u>
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* From the Auditor Skills Profile.

Professional Development Curriculum

DOE/OIG Office of Audits

GS-7/9

GS-11/12

GS/GM-13/14

GM-15

AUDITOR SKILLS PROFILE
AUDITORS, GS/GM-511-7/14

**GRADE LEVEL AT WHICH
SKILL SHOULD BE OBTAINED**

CODE	TRAINING SUBJECT MATTER	GS 7/9/11	GS 12/13*	GS/GM 14*
A	GENERAL			
A1	Federal Government Overview	X		
A2	Federal Financial Overview	X		
A3	DOE Organization, Mission, Programs, and Respon.	X		
A4	OIG Organization, Mission, Policies and Procedures	X		
A5	Inspector General Act and Related OMB Circulars	X		
A6	Ethics/Conflict of Interest	X		
B	AUDITING POLICIES AND PROCEDURES			
B1	Generally Accepted Govt. Auditing Standards (GAGAS)	X		
B2	Types and Phases of Government Audits	X		
B3	Audit Planning	X		
B4	Internal Controls	X		
B5	Evidence	X		
B6	Workpaper Design and Preparation	X		
B7	Elements of Audit Findings	X		
B8	Conducting Audit Surveys	X		
B9	Developing Audit Programs	X		
B10	Audit Reporting Requirements	X		
B11	Audit Follow-up and Resolution	X		
B12	Financial Statement Auditing	X		
B13	Operational and Performance Auditing	X		
B14	Referencing		X	
C	AUDIT METHODOLOGY			
C1	Flow Charts	X		
C2	Statistical Sampling	X		
C3	Analytical Techniques	X		
C4	Legislative History and Regulatory Research	X		
D	WRITTEN COMMUNICATION			
D1	Writing Audit Findings	X		
D2	Writing Audit Reports		X	
D3	Reviewing and Editing Audit Reports		X	
D4	Writing Memorandums, Letters, etc.	X		

* Auditors at these grade levels should continue to pursue training opportunities, at the intermediate and advanced levels, in each of the major areas listed above that are relevant to their job responsibilities.

AUDITOR SKILLS PROFILE
AUDITORS, GS/GM-511-7/14

**GRADE LEVEL AT WHICH
SKILL SHOULD BE OBTAINED**

CODE	TRAINING SUBJECT MATTER	GS 7/9/11	GS 12/13*	GS/GM 14*
E	NON-WRITTEN COMMUNICATION			
E1	Interviewing	X		
E2	Conducting Entrance and Exit conferences	X		
E3	Oral Presentations	X		
E4	Conducting Meetings with Agency Senior Management			X
F	AUDIT MANAGEMENT			
F1	Supervision		X	
F2	Workload Planning		X	
F3	Audit Office Resource Management			X
F4	Organizational Development			X
F5	Quality Control			X
F6	Equal Employment Opportunity	X		
G	FRAUD, WASTE, AND ABUSE AWARENESS			
G1	Fraud Awareness and Reporting	X		
G2	Legal Implications of Audits	X		
G3	Statements on Auditing Standards (SAS)	X		
H	AUTOMATED DATA PROCESSING			
H1	ADP Concepts	X		
H2	Internal Controls in ADP Systems	X		
H3	Auditing ADP Systems	X		
H4	Auditing Microcomputers	X		
H5	Using Microcomputers	X		
H6	Audit Software	X		
I	MANAGEMENT DEVELOPMENT			
I1	Management and Leadership Skills			X

**U.S. DEPARTMENT OF ENERGY — OFFICE OF INSPECTOR GENERAL
ON-THE-JOB TRAINING (OJT) PERFORMANCE RECORD**

<u>Name</u>	<u>Duty Station</u>	<u>Grade</u>
<u>Element/Task</u>	<u>Date</u>	<u>Supervisor's</u> <u>Initials</u>
		<u>Performance</u> <u>Satis. Unsatis.</u>
1. PLANNING/Develop Audit Steps		
2. PLANNING/Determine Criteria		
3. PLANNING/Assist Audit Survey		
4. PLANNING/Suggest Audit Leads		
5. DATA ACQ/Follow Audit Program		
6. DATA ACQ/Convincing Evidence		
7. DATA ACQ/Interview Questions		
8. DATA ACQ/Prepare Workpapers		
9. DATA ANAL/Comp. Spreadsheet		
10. DATA ANAL/Finding Elements		
11. WRITING/Interview Write-ups		
12. WRITING/Comp. Word processing		
13. WRITING/Workpaper Summaries		
14. WRITING/Draft Report Segments		
15. ORAL COM/Work Status Briefing		
16. ORAL COM/Interview Questions		
17. ORAL COM/Work by Telephone		
18. RELATIONS/Follow Protocol		

EXPLANATION OF OJT ELEMENTS/TASKS**PLANNING**

1. **Develop Audit Steps.** A new auditor may demonstrate proficiency in developing audit steps by gathering information as directed by the supervisor for completing an acceptable audit program or by writing steps approved by the supervisor for carrying out an audit program segment.
2. **Determine Criteria.** The new auditor should identify and obtain the applicable law(s), regulations or other criteria pertinent to the audit assignment.
3. **Assist Audit Survey.** To understand the process of preliminary testing and the role of the audit survey (go/no go decisions, narrowing audit goals and objectives, etc.), the new auditor should assist a senior auditor in successfully completing an audit survey.
4. **Suggest Audit Leads.** To demonstrate alertness to audit leads and to appreciate the role of audit leads in workload planning, the new auditor should prepare an audit profile which is acceptable to the supervisor.

DATA ACQUISITION

5. **Follow Audit Program.** The new auditor should successfully acquire data through interviews, records reviews or other means to fulfill the intent of an audit program.
6. **Convincing Evidence.** The new auditor should demonstrate an appreciation of the distinction between weak evidence (interviews) and strong evidence (original documentation) and should acquire sufficient evidence to convince the supervisor that adequate support exists for assertions, conclusions, etc.
7. **Interview Questions.** The new auditor should develop logical, probing interview questions which are approved by the supervisor.
8. **Prepare Workpapers.** The new auditor should prepare workpapers with appropriate references to the purpose, scope, source, and conclusion, with necessary cross-indexing to other workpapers where applicable.

DATA ANALYSIS

9. **Computerized Spreadsheet.** The new auditor should demonstrate the ability to prepare a spreadsheet using data acquired during an actual audit. To be proficient, the auditor must be able to sort and print the data for various analyses appropriate to the audit.
10. **Finding Elements.** The new auditor should demonstrate a good working understanding of the condition, cause, criteria, and effect which comprise an audit finding. The new auditor may either identify the elements in existing written products or successfully outline the correct elements in an audit profile sheet or a draft finding charge paragraph.

WRITING

11. Interview Write-ups. The new auditor should demonstrate to the supervisor an ability to write an interview memorandum succinctly, accurately, logically, and in good format.
12. Computerized Word Processing. The new auditor should successfully produce a coherent, relatively error-free written product (memorandum of record, workpaper summary, audit profile sheet, draft report segment, etc.) and demonstrate an ability to use a word processing program to effectively move text and otherwise edit.
13. Workpaper Summaries. The new auditor should prepare a brief, coherent and accurate summary for a workpaper bundle.
14. Draft Report Segments. The new auditor should write a draft report segment (Introduction and Scope, Observations and Conclusions, etc.), which is accepted by the appraising official.

ORAL COMMUNICATIONS

15. Work Status Briefing. The new auditor should give an effective briefing to the appraising official or other higher level Office of Audits officials on the new auditor's progress on an assigned work segment. Although a formal presentation is not necessary, the briefing should be concise and well organized.
16. Interview Questions. The new auditor should effectively ask planned interview questions and demonstrate an ability to ask appropriate follow-up questions.
17. Work by Telephone. The new auditor should demonstrate an ability to set up meetings, ask simple follow-up questions, and otherwise effectively use the telephone in accomplishing those small work tasks for which face-to-face meetings are not appropriate.

WORKING RELATIONSHIPS

18. Follow Protocol. The new auditor should demonstrate a willingness and ability to follow protocol through adequate coordination with supervisors, audit liaisons, and other designated points of audit contact. The auditor should also exhibit alertness, tact, objectivity, appropriate deference to superiors, respect for the views and opinions of others, and professional skepticism.

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